In the
Supreme Court of the United States
OCTOBER TERM, 1942

No. 319

FIDELITY ASSURANCE ASSOCIATION, a corporation, Debtor, and CENTRAL TRUST COMPANY, Trustee for Fidelity Assurance Association,

Petitioners,

v.

EDGAR B. SIMS, Auditor of the State of West Virginia, and Ex Officio Insurance Commissioner of the State of West Virginia; ROSS B. THOMAS and H. ISAIAH SMITH, West Virginia State Court Receivers; BANKING COMMISSION OF WISCONSIN; CHAS. R. FISCHER, Commissioner of Insurance and Permanent Receiver for debtor corporation in and for the State of Iowa; JOHN B. GONTRUM, Insurance Commissioner of the State of Maryland; DEWEY S. GODFREY, Missouri State Court Receiver; L. H. BROOKS, Trustee, FREDERICK E. KE and A. L. GOLDBERG, Jr., Trustee; and SECURITIES AND EXCHANGE COMMISSION,

Respondents.

ON WRIT OF CERTIORARI
TO THE UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE FOURTH CIRCUIT

BRIEF OF RESPONDENTS, BANKING COMMISSION OF WISCONSIN AND CHAS. R. FISCHER, COMMISSIONER OF INSURANCE AND PERMANENT RECEIVER FOR THE STATE OF IOWA

JOHN E. MARTIN,
Attorney General, State of Wisconsin
J. JAMES WARD RECTOR
Deputy Attorney General, State of Wisconsin
RICKARD H. LAURITZEN,
Assistant Attorney General, State of Wisconsin
Attorneys for Respondent
Banking Commission of Wisconsin
JOHN M. RANKIN,
Attorney General, State of Iowa
FLOYD PHILBRICK,
First Assistant Attorney General, State of Iowa
CARL J. STEPHENS
BEN C. BUCKINGHAM
Attorneys for Respondent,
Charles R. Fischer, Commissioner of Insurance
and Permanent Receiver for Debtor Corporation
In and For the State of Iowa

THE GILMAN PRESS, MADISON, WISCONSIN

INDEX

CITATIONS

CASES

STATUTES

In the

Supreme Court of the United States

OCTOBER TERM, 1942

No. 319

FIDELITY ASSURANCE ASSOCIATION, a corporation, Debtor, and CENTRAL TRUST COMPANY, Trustee for Fidelity Assurance Association,

Petitioners,

v.

EDGAR B. SIMS, Auditor of the State of West Virginia, and Ex-Officio Insurance Commissioner of the State of West Virginia; ROSS B. THOMAS and H. ISAIAH SMITH, West Virginia State Court Receivers; BANKING COMMISSION OF WISCONSIN; CHAS. R. FISCHER, Commissioner of Insurance and Permanent Receiver for debtor corporation in and for the State of Iowa; JOHN B. GONTRUM, Insurance Commissioner of the State of Maryland; DEWEY S. GODFREY, Missouri State Court Receiver; L. H. BROOKS, Trustee, FREDERIC LEAKE and A. L. GOLDBERG, Jr., Trustee; and SECURITIES AND EXCHANGE COMMISSION,

Respondents.

ON WRIT OF CERTIORARI
TO THE UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE FOURTH CIRCUIT

BRIEF OF RESPONDENTS, BANKING COMMISSION OF WISCONSIN AND CHAS. R. FISCHER, COMMISSIONER OF INSURANCE AND PERMANENT RECEIVER FOR THE STATE OF IOWA

On October 12, 1942 this court granted certiorari to review a decree of the Circuit Court of Appeals for the Fourth Circuit, reversing an order of the United States District Court for the Southern District of West Virginia dated January 5, 1942. The order of the District Court had sustained the petition for reorganization of Fidelity Assurance Association, the debtor, and had overruled certain motions of the respondents Insurance Commissioner of Maryland, L. H. Brooks, Trustee, Frederic Leake and A. L.

Goldberg, Jr., Trustee, and Edgar E. Sims, Auditor of the State of West Virginia and ex-officio Insurance Commissioner of the State of West Virginia, Ross B. Thomas and H. Isaiah Smith, West Virginia State Court Receivers.

OPINIONS BELOW

The opinion of the District Court is reported in 42 F. Supp. 973. The opinion of the Circuit Court of Appeals is reported in 129 F. (2d) 442.

JURISDICTION

The jurisdiction of this court rests on Section 240 (a) of the Judicial Code (28 U. S. C. A., sec. 347) and Section 24 (c) of the Bankruptcy Act (11 U. S. C. A., sec. 47 (c)).

STATEMENT OF THE CASE

A. Nature of the case and the procedural facts

On June 6, 1941 Fidelity Assurance Association, the debtor herein, filed a petition for reorganization under Chapter X of the Bankruptcy Act in the United States District Court for the Southern District of West Virginia (R. 4-9), and on June 6, 1941 that court entered its order approving the petition as properly filed (R. 1-4). Thereafter the Banking Commission of Wisconsin (hereinafter referred to as the Wisconsin respondent) filed its answer controverting said petition (R. 48-56), and Charles R. Fischer, Commissioner of Insurance and Permanent Receiver for Debtor Corporation in and for the State of Iowa (hereinafter referred to as the Iowa respondent) also filed his answer controverting said petition (R. 118-124). Answers controverting debtor's petition were also filed by

the respondents Edgar B. Sims, Auditor of the State of West Virginia and ex-officio Insurance Commissioner of the State of West Virginia, and H. Isaiah Smith and Ross B. Thomas, West Virginia State Court Receivers (hereinafter referred to as the West Virginia respondents) (R. 58-83); L. H. Brooks, Trustee, Frederic Leake and A. L. Goldberg, Jr., Trustee (hereinafter referred to as the Tennessee respondents) (R. 96-102); and Dewey S. Godfrey, Receiver in the State of Missouri (hereinafter referred to as the Missouri respondent) (R. 91-93). The Insurance Commissioner of Maryland (hereinafter referred to as the Maryland respondent) appeared specially and filed motions to strike out or rescind certain orders entered in the District Court on June 6, June 10 and August 9, 1941, directing certain state officials, including the Maryland respondent, to turn over certain property to the federal trustee and enjoining them in certain particulars (R. 124). The West Virginia respondents (R. 93-96; 124-127) and the Tennessee respondents (R. 128-130) also filed similar motions in the District Court with respect to said orders.

A trial of the issues presented by debtor's petition and the controverting answers and motions of said respondents was had in the District Court. On January 5, 1942 the District Court entered its order formally approving the debtor's petition for reorganization and overruling the motions of the West Virginia, Tennessee and Maryland respondents relative to the District Court's orders of June 6, June 10 and August 9, 1941.

The respondents appealed from said order to the Circuit Court of Appeals for the Fourth Circuit, and on June 16, 1942 the Circuit Court reversed the order of the District

Court and directed that debtor's petition for reorganization should be dismissed.

The debtor and the federal trustee petitioned to this court for a writ of certiorari to the Circuit Court of Appeals, and the writ was granted under date of October 12, 1942.

B. Respondents' joint statement of facts

This statement is made by and on behalf of all of the respondents herein except the Securities and Exchange Commission and for convenience is incorporated in this, the brief of the Wisconsin and Iowa respondents. It is designed to give as complete a picture as practicable, from the record herein, of the debtor's business and of these proceedings as affect the interests, generally, of all such respondents. Additional statements of fact as particularly affect the interests of each of the several respondents will be found in their respective briefs.

The pleadings and certain portions of the testimony have by stipulation been printed as the record in this court. The original exhibits have not been printed and are on file in this court. The references herein to the pleadings and testimony will be to the pages of the printed record in this court, and the references to exhibits will be to the original exhibit numbers of such exhibits together with the page of the record as printed in this court where such exhibits are admitted in evidence. In some instances the record as printed omits reference to the introduction of exhibits, and in such cases we have referred to the page of the original transcript where the exhibit is admitted in evidence as "R. — (original))." Certain exhibits and other material are printed in the Appendix to this brief, to which reference will be made as "(App. —)."

1. Debtor's corporate charter and amendments thereto

Fidelity Assurance Association was organized under the name of Fidelity Investment and Loan Association under the laws of West Virginia on April 11, 1911. In 1912 its corporate purposes were enlarged to include the business of soliciting or receiving payments on annuity contracts, and by virtue of this amendment it became subject to the provisions of Art. 9 of Ch. 33 of the Code of West Virginia relating to the business of selling "annuity contracts" and was licensed and supervised by the Insurance Commissioner of West Virginia as an annuity company until January 1, 1940. Art. 9, Ch. 33, the Annuity Company Law, was repealed by Ch. 46, Acts of the West Virginia Legislature, passed March 8, 1941, effective ninety days thereafter. Other amendments to the articles were made in 1926, 1929 and 1931, all as shown by Ex. 20 (R. 398).

Amendment of December 31, 1940

On December 31, 1940 the debtor amended its charter, changing its name from Fidelity Investment Association to Fidelity Assurance Association. It also struck out Art. 3 of its charter as amended in December, 1912, which contained a statement of its various corporate purposes as above outlined and inserted in lieu thereof, as the complete statement of its corporate purpose, the following:

> "To issue insurance upon the lives of persons and every insurance appertaining thereto and connected therewith, and to grant, purchase and dispose of annuities." (Ex. 24, R. 437, App. 76)

Amendment of January 24, 1941

On January 24, 1941 the stockholders of the debtor further amended its charter reducing its authorized capitalization to $1,000,000 of common stock of a par value of $8 per share, the total outstanding stock to be reduced to $2,210,744 of common stock with a par value of $8 per share. In the resolution of amendment it was stated that the reason for this reduction was that at that time the company was "qualified and admitted to transact a life insurance business in the state of West Virginia only" and that it was desired to further extend the territory in which the company might operate such business and that it was necessary that the stock of the company should be common stock of all one class and be reduced to such an amount as would leave a surplus after deducting those assets of the company which were not admitted as such by the insurance departments of the various states in which it was desired to do business. (Ex. 20, R. 398) A more detailed statement of the circumstances of the debtor's conversion into a life insurance company will be made later on in this statement of facts.

2. The "Fidelity plan" in operation from December, 1912 to December 31, 1940

Up to December 31, 1940 the debtor's business was that of selling its so-called investment or annuity contracts. At one time it was licensed in 29 states. Specimens of the various contracts which it issued comprise Exs. 1 to 5 (R. 170 (original)) inclusive. From time to time the form of the contracts was changed in certain particulars, but generally speaking, the "Fidelity Plan" provided for the issuance and sale of certificates whereby the purchaser

agreed to make monthly payments, in most cases for 120 months, of a definite sum of money and Fidelity agreed to return to the purchaser at the end of the monthly payment period a certain sum of money known as the "face amount" of the contract. This sum was to be paid in various annual, quarterly, monthly or other periods in accordance with the particular optional settlement plan elected by the contract holder. A sum considerably smaller than the "face amount" would be paid in a lump sum at the end of the ten year period, but after the expiration of the "waiting period" as referred to in the District Court's opinion. Each series of contracts contains extremely detailed provisions as to the rights of the contract holders with respect to payments, cash surrender values, lapsation upon failure to make payments and various optional plans of settlement. The contracts did not provide for any cash surrender or loan value until from ten to sixteen monthly payments had been made (p. 81 of Ex. 6, R. 1749 (original)) and if the contracts were lapsed at any time during these periods the contract holder forfeited to Fidelity all of the payments made. (Exs. 1 to 5, inclusive, R. 170 (original)) The contracts had to be carried for a period varying from six to nine years before the cash surrender value would be equal to the payments which had been made (p. 82 of Ex. 6, R. 1749 (original)). Exhibit 6 comprises the Report of the Securities and Exchange Commission on Companies Issuing Face Amount Installment Certificates made pursuant to Section 30 of the Public Utility Holding Company Act of 1935, hereinafter sometimes referred to as "SEC report." After all of the payments had been completed there was a waiting period varying from four to fourteen

months before payments to the contract holders would commence (p. 80 of Ex. 6, R. 1749 (original)).

Prior to 1922 certain contracts known as the "Old ten-year Series" and Series D and C had been sold but apparently few if any of these are now outstanding (R. 304). At this time the company's total assets were only about $2,000,000 (R. 307). In 1921 the sale of the special income contract (Ex. 1, R. 170 (original)) commenced and this continued up to 1925, but there are only about 900 holders of these today (R. 304). This contract was discontinued because of litigation with the state of Illinois, the Secretary of State having objected to it on the ground that it was possibly misleading (R. 305-306) and the "Special Annuity Contract" (Ex. 2, R. 170 (original)) was formulated (R. 306) and sold up to 1932. This was a period of tremendous growth for the company, its assets by 1932 amounting to in excess of $25,000,000 (R. 308). In 1932 the "Special Income Contract" was formulated and this was sold up to 1934.

In 1934 Fidelity commenced the issuance of the so-called Series B contracts and the sale of these contracts comprised practically its entire volume up to the time when it suspended the business of selling contracts late in 1940. The Series B contracts were issued in two types—one the regular form and the other having an insurance protection feature which was set forth in sec. 6 of the contract and made operative at the election of the purchaser (Ex. 4, R. 170 (original)). The insurance feature provided, for an additional charge, that upon the death of the purchaser prior to the maturity of the contract a sum would be provided sufficient to pay the contract to maturity or to pro-

vide a so-called commuted value of a paid-up contract to the purchaser's estate. According to the SEC report (p. 114 of Ex. 6, R. 1749 (original)), the yield on the Series B contracts was as follows:

Mode of Settlement	With Insurance Value	With Insurance Yield Percent	Without Insurance Value	Without Insurance Yield Percent
(1) Cash surrender value at end of 126 (total) monthly-installment payments	$1,015	1.34	$1,075	2.41
(2) Cash maturity value 129 months after due date of first monthly installment	1,030	1.55	1,090	2.56
(3) 10 annual payments, after maturity, of $125 each	1,250	2.82	(a)	3.38

Seventy-five per cent of the Series B contracts sold carried the insurance feature (R. 681). Series D contracts were sold in Ohio, Kentucky and Alabama because the authorities in those states would not permit the sale of the Series B contracts with insurance unless the company qualified as a life insurance company (R. 315).

(a) Amount not shown

3. Fidelity a "compulsory savings" plan

As has been shown the net return to investors under the Fidelity plan was not large and they stood to lose all of their investment if they did not make at least twelve monthly payments and it was not until they had paid continuously for from six to nine years that the contracts had a cash surrender value equal to the amount of the payments made. Furthermore, it appears that only 5.29% of the persons who purchased Fidelity contracts carried them to maturity (R. 388). The record amply bears out the statement in the SEC report (p. 106 of Ex. 6, R. 1749 (original)) that "The experience of purchasers of the Association's investment certificates appears to be unsatisfactory as a whole." According to that report the loss to contract holders by reason of surrender and lapsation during the ten year period, 1927-1936, was $7,510,000 (p. 92 of Ex. 6, R. 1749 (original)). During that period the certificates which matured equaled only 14% of the amount of certificates in force at the beginning of the period (p. 11 of Ex. 6, R. 1749 (original)). Forty-seven per cent of the purchasers failed to carry the contracts for as much as one year (R. 783). F. J. McNulty, the debtor's vice-president, stated he could not say whether or not more than 2% of all those who had paid their money into Fidelity had gotten it out at maturity (R. 391).

Despite these figures, which are not disputed, those of debtor's officers who testified during the proceeding stoutly maintained their faith in the Fidelity plan as providing a means for small wage earners in the United States to put in operation a beneficial plan of savings. The lapsation losses, far from being regarded as in derogation of the "Fidelity plan," were regarded as providing a spur and

incentive to the contract holders to continue payments, which were lacking in other investment plans. John Marshall, Sr., a director for twenty years, chairman of the Board for several years, general counsel, and voting trustee for the majority of stock (R. 410), stated that he understood from Mr. Paull (his father-in-law and one of the original founders) that he "thought there was a great need (for the Fidelity plan) because of his banking experience; that a great many people opened savings accounts but did not continue them" (R. 417).

D. A. Burt, a director, stated that even though the contracts did not have a cash surrender value equal to the amount of payments until they had been carried for many years, since they were sold with that understanding as expressed in the contract, he didn't "think there is any injustice done to anyone" (R. 710-711). The fact that only 5% of the contract holders carried their contracts to maturity did not alter his views (R. 712). The fact that "every month I got a little reminder on my desk that it was time for me to pay $10 or $7.50 into this Fidelity contract" seemed to him to be a very favorable factor in the plan (R. 713). As the District Court interpreted Mr. Burt's testimony:

> "It is not so much a question of a reminder as a question of compulsion on the part of the contract holder to pay or lose what he had paid" (R. 713).

The element of compulsion as being the salient feature of the plan was emphasized by L. H. Pulfer, who had been vice-president of Fidelity in charge of recruiting and building up the sales organization and who was later in charge of sales in the Chicago territory which was composed of a

number of states (R. 513). He stated that the principal appeal of the plan was "it offered that element of compulsion which would get a man to do that particular thing which otherwise he probably would not do" (R. 523). Without further elaboration it may be stated that the sole economic justification for the existence of Fidelity seems, in the opinion of its officers and principals, to be that it offered a plan of "compulsory savings" (R. 557). It was particularly emphasized that nothing advantageous was claimed by way of interest return (R. 523, 557).

The SEC report which comprises Exhibit 6 of the record herein deals in the greatest of detail with Fidelity's business and also with the business of the two other companies which are apparently the only other concerns which have been engaged in any substantial way in this peculiar type of business in this country. It may be stated categorically that an examination of this report and the record in the present case reveals conclusively that the experience of investors with Fidelity and with the other companies selling these certificates has been anything but a happy one. Tables on pp. 112-113 of Ex. 6 compare the relative advantage to an investor over a ten year period in placing like sums at like intervals in a savings account, in United States Savings Bonds and in a Fidelity contract. Considering the fact that the greater percentage of Fidelity's purchasers lapsed their contracts either in the first year or in the first few years, and thus lost all or a great part of their investment, the advantage of either of the first two forms of investment over that of Fidelity is obvious.

4. The sale of the contracts

From 1925 to 1934 Fidelity's sales were in the hands of a corporation known as National Sales Agency, Inc. (R. 514) which was owned by Fred King and A. L. King (R. 514) who were also dominant figures in Fidelity. Prior to 1925 National Sales Agency handled sales in the eastern territory and a firm known as Irving and Sisson, the western territory. Ex. 34 (R. 515) shows the number and geographical distribution of contracts outstanding as of April 10, 1941. This exhibit indicates that as of that date there were 87,999 contracts outstanding, but it was testified by Mr. McNulty, the secretary and vice-president of the company (R. 407), that on that date the number of "active" contracts (meaning those upon which regular payments were being continued) was between 22,000 and 25,000. According to Ex. 34 (R. 515) the cash liabilities on the contracts outstanding as of April 10, 1941 were $23,475,068.67.

In the operation of the "Fidelity plan" a substantial part of the contract holders' payments were applied to "loading" to pay sales expense. This "loading" amounted to the entire first eight months' payments on the Series B contracts, and over the entire life of the Series B contracts, 13.7% of total payments on insured contracts and 9% of total payments on uninsured contracts (p. 82 of Ex. 6, R. 1749 (original)). In 1935, when Carroll D. Evans took over the sales management, the company had about 20 offices and 400 salesmen and the volume of sales was $1,000,000 of face amount per month (R. 921-922). From 1935 to 1940 the offices increased to about sixty in number with 1,800 salesmen in all (R. 926). The turnover of salesmen was extremely high, more than 80% per year (R. 927), and the recruiting of salesmen was one of the most important

phases of the company's activities (R. 927-929). In order to get one acceptable producer it was necessary to interview 100 men (R. 929).

Despite the loading charges, National Sales Agency, Inc. became indebted to Fidelity in the amount of $1,000,000 by reason of advances made by Fidelity to that corporation upon unearned commissions (R. 384). This debt was never repaid and was transferred to certain subsidiary corporations of Fidelity (R. 769-770). After 1934 the company organized its own agency division to take over the sales which were formerly in the hands of National Sales Agency, Inc. (R. 515). Various sales officers of Fidelity who testified in this proceeding insisted that impressive and expensive offices in the principal places were Fidelity operated were a necessity in order that prospective salesmen might be favorably impressed (R. 923-924). However, despite constantly increased sales effort and expense the company consistently lost money.

The debtor's petition for reorganization (R. 7) alleges that it is suffering an annual loss of $250,000 and that this rate of loss will continue and probably increase unless the earnings or its invested securities should increase far in excess of the present rate of income. Prior to June 6, 1941, the date of filing of the petition for reorganization, all of the Fidelity sales offices had been closed and its sales organization completely dissipated and lost (R. 346-349). In 1938 or in the early part of 1939 the company's license to do business was suspended in most of the states where it did business (R. 393), and it is not now licensed in any state. It was estimated that it would take around $500,000 to recruit a new sales force which would provide adequate sales to continue operations (R. 933-934).

5. State deposits the basis for sales

The fact that Fidelity was subject to strict regulatory laws and had deposited securities thereunder to secure its obligations was a most potent sales point. The deposit laws were "the fundamental selling principle" (R. 917). The selling point in West Virginia was that "that fund would be available and under the control of the State Auditor in the event of any liquidation of the company," according to Mr. Risley, the president (R. 917). The West Virginia law "was one of the features that was stressed" (R. 921). The sales pamphlets and reports sent to contract holders made detailed reference to the state laws. In Ex. 37 (R. 852 (original)), a sales pamphlet showing the manner in which Fidelity purported to select its portfolio of investments, it was said that the securities selected were "deposited with state departments for the exclusive protection of contract holders." In Ex. 38 (R. 853 (original)) under the heading, "The exacting law under which the Association operates," sec. 3, Art. 9, Ch. 33 of the West Virginia Code was quoted. Ex. 39 (R. 853 (original)) states, under the company's financial statement, the following:

> "Securities deposited with state departments in accordance with legal requirements of each state in which we operate."

Ex. 106 (R. 1034) used in Wisconsin, contains pictures of the state capitol there and quotes portions of the Wisconsin deposit law. The company also used brochures showing pictures of the vault in the West Virginia state capitol (R. 605) and, according to Auditor Sims, sought to give out "that the state of West Virginia was behind the contracts" (R. 605-606).

6. The supervision of Fidelity by Edgar B. Sims, Auditor and Ex Officio Insurance Commissioner of West Virginia

It is in its relationship with the Auditor and ex-officio Insurance Commissioner of West Virginia that the long existing moribund condition of Fidelity is most clearly disclosed. Edgar B. Sims first was elected to this office in 1933 and he still holds it (R. 434). Upon his becoming acquainted with the affairs of Fidelity which were under his jurisdiction, he found that "the company was in the red in market values about $7,000,000" (R. 442). Auditor Sims had general supervising jurisdiction over the company by virtue of Art. 9, Ch. 33, West Virginia Code (repealed March 8, 1941) and under sec. 3 thereof, he, as Insurance Commissioner, was to require and approve the deposit with the State Treasurer by Fidelity, of bonds and securities to be held in trust for the benefit of its contract holders located in West Virginia to an amount equal to the cash liability of West Virginia contract holders. In addition he was to require and approve a deposit in trust for the benefit of contract holders located in states other than West Virginia to the extent that the laws of such states did not provide for a deposit equal or greater than that provided for by the laws of West Virginia. Soon after taking office he discovered that Fidelity's liabilities far exceeded the market value of its assets and also discovered advances by Fidelity to National Sales Agency, Inc. of $957,000 (R. 440). He was assured, however, that the note was perfectly good (R. 440). He told Fidelity that it must operate within the loadings provided by the contracts for commissions so that this note would be reduced. The officers told him that they were obeying him but they did not obey (R. 440) and he found that the advances had increased by $90,000 by the

end of the year (R. 440). In 1934 he insisted that Fidelity should take over the sales agency bank account or he would close Fidelity's business and the company complied with this order (R. 441). He called a meeting of the directors in Washington, D. C., and insisted that with the $300,000 to $500,000 per month which the contract holders were paying in Fidelity should buy bonds that had not defaulted during the depression in interest or principal, which were being sold at a discount at that time (R. 441). This policy appeared to work satisfactorily for a time due to a great rise in market prices, so that Auditor Sims could state that whereas the company was in the red in market values in 1933 about $7,000,000 "in market value today it is in the red only 2¼ million dollars" (R. 442). Auditor Sims ordered the company to cease renting expensive offices for the various sales managers but he had extreme difficulty in having this done (R. 442). He stated that the only reason the company was able to exist during the period from 1933 to 1940 was by the purchase of securities on a low market which had subsequently risen in value (R. 444), that the only way that the contracts could be sold were by means of what is known as "high pressure salesmanship" and that the expense of selling by this method was too great (R. 444).

Auditor Sims stated that, based upon his experience as auditor and his knowledge of the affairs of Fidelity, he did not believe the company could be reorganized in West Virginia "with the corpse of this one" (R. 449-450). He doubted very sincerely whether anyone could operate a face amount certificate company successfully in view of present economic conditions (R. 450). He believed that even with good management Fidelity would have been

unsuccessful because "they promised too much in their contracts and the economic change in interest rates, money rates, wouldn't stand that" (R. 453). The present outstanding contracts would have to be modified and he believed that the "structure of the company economically and financially was unsound from the beginning" (R. 453-454). Even if it was run economically he felt it was condemned, stating that, "I think they were quarreling with Ray's arithmetic all the time back there" (R. 454). He had thought that the company could be mutualized and turned over to the contract holders because there is nothing left for the stockholders, but the sort of plan he had hoped to work out was very thin and nebulous (R. 457). The situation apparently appeared desperate to Auditor Sims in November and December, 1940. At that time he ordered the stock trusteed in the hands of disinterested parties, but they did not answer his letter (R. 458). Finally he filed suit through the office of the Attorney General of West Virginia (R. 459) to which further reference will be made.

7. Regulation of Fidelity by states other than West Virginia

Fidelity was at one time licensed in 29 states and each of these states had regulatory laws governing the operation of its business (R. 347). Fifteen of the states in which it did business, including West Virginia, had laws requiring a deposit of securities to secure its outstanding contracts and the remainder of the states did not require a deposit, but the contracts sold in those states were secured by the deposit made with the state of West Virginia (R. 348). Ex. 48 (R. 1116 (original)) contains a list of the states having deposit laws, the market value of securities on deposit in each (as of June 6, 1941), the "net reserve liability" in

each and the "net cash liability" in each which is (as of April 10, 1941), according to Fidelity's figures, as follows:

	Deposits by States as of June 6, 1941	Liabilities by States as of April 10, 1941	
	Market Value	Net Reserve Liability	Net Cash Liability
Ala.	$ 32,555.16	$ 32,267.31	$ 31,346.71
Del.	293,790.63	300,074.88	290,175.36
Ill.	3,759,894.00	4,368,348.52	4,225,790.75
Ind.	162,863.44	398,336.17	386,173.45
Iowa	45,082.50	35,332.03	34,478.27
Kansas	83,337.50	111,530.90	108,784.89
Ky.	86,712.50	95,376.98	92,690.42
Md.	470,806.25	508,163.70	492,552.24
Mo.	861,100.62	807,263.78	786,988.86
Ohio	509,573.44	2,439,364.17	2,360,418.70
Pa.	232,591.57	4,816,175.07	4,668,582.25
Tenn.	196,574.38	206,879.70	200,504.97
Va.	27,703.13	572,585.25	557,809.19
West Va.	10,674,696.08	7,121,651.33	6,896,393.88
Wis.	2,619,399.07	2,408,301.57	2,342,978.73
	$20,056,680.27	$24,221,651.36	$23,475,668.67

Ex. 48 shows that the company had certain securities which are not on deposit anywhere in an amount of $556,467.51 but most of these would not be eligible for deposit under any of the state laws (R. 816). It should be stated that no direct testimony was introduced as to the market value of debtor's assets. Debtor made up its schedules from audit reports made by outside accountants who did not testify and whose methods of ascertaining values is not shown. With respect to assets other than securities, no attempt was made to place a valuation thereon in the pro-

ceedings. Thus, while we use the debtor's figures, such as those above, it should be understood that the respondents do not consider themselves bound by such figures as reflecting market or other values. The record would indicate that actual values are, in a number of instances, a great deal lower than indicated in the various schedules in evidence, and it is difficult, if not impossible, to state the true situation as to the degree of debtor's insolvency from the record.

In each state in which it did business, whether the state required a deposit or not, Fidelity was subject to special provisions of law applicable either to insurance corporations, banking corporations, building and loan associations, investment companies or other companies whose business is affected with a public interest. As we have shown, Fidelity, prior to its becoming chartered as a life insurance company, operated under the so-called Annuity Company Law of West Virginia, now repealed. In the states in which it did business it qualified with and was regulated by various state departments, in some states the Insurance Department, in some the Banking Commission and in others the Securities Department (R. 348). In the states which required deposits, as listed above, qualification and regulation was by the various departments as follows:

State	Department	
Alabama	Securities Commission	(R. 348)
Delaware	Banking Commissioner	(R. 349)
Illinois	Secretary of State	(R. 350)
Indiana	Auditor prior to 1934, Securities Commission after 1934	(R. 353)
Iowa	Securities Department and Insurance Commissioner	(R. 353)

Kansas	State Corporation Commission by the Securities Commissioner	(R. 354)
Kentucky	Division of Securities, Department of Banking and Securities	(R. 355)
Maryland	Insurance Department	(R. 356)
Missouri	Commissioner of Securities	(R. 357)
Ohio	Superintendent of Insurance	(R. 359)
Pennsylvania	Formerly Banking Department now Securities Commissioner	(R. 360)
Tennessee	Department of Insurance and Banking	(R. 361)
Virginia	State Corporation Commission	(R. 363)
Wisconsin	Banking Commission (also subject to registration with Securities Department, Ch. 189, Wis. Stats.)	(R. 364)

With respect to states which did not have deposit laws, the regulatory jurisdiction was as follows:

State	Department	
Dist. of Columbia	No regulation	(R. 371)
Arkansas	Securities Division, Railroad Commission	(R. 370)
Florida	Securities Commission	(R. 371)
Georgia	Securities Commission	(R. 371)
Louisiana	Securities Commission	(R. 371)
Michigan	Department of Insurance	(R. 371)
Mississippi	Secretary of State	(R. 371)

Maine	Commissioner of Securities, Department of Commerce	(R. 372)
New Jersey	Department of Insurance and Banking	(R. 372)
North Carolina	Securities Department	(R. 372)
North. Dakota	Securities Department	(R. 372)
Oklahoma	Securities Division, State Banking Department	(R. 372)
South Dakota	Securities Department	(R. 373)
South Carolina	Securities Commission	(R. 373)

The laws of the various states providing for regulation of such concerns as Fidelity, placed it in varying classifications. In Wisconsin it was subject to all of the provisions of law with respect to the supervision, control and conditions upon which foreign building and loan associations are permitted to do business in that state. Sec. 216.02 Wis. Stats. Registration of its contracts was also compelled under the Wisconsin Securities Law, Ch. 189 Wis. Stats. In Kansas, South Dakota and Mississippi the statutes define a business such as that done by Fidelity as the doing of a building and loan association business, Ch. 17, Art. 10, sec. 17-1047, Corrick's General Statutes of Kansas, Ann., 1935; Tit. 7, Ch. 7.01, South Dakota Code, 1939; Ch. 96, sec. 4300, Hemingway's Ann. Code of Mississippi. In certain other of the states Fidelity was compelled to register its contracts as securities under securities laws which in some instances provided for a deposit. The deposit laws of the various states provide in most cases for a deposit in trust for the benefit and security of contract holders located therein and provide for the liquidation of these funds in the various states when-

ever Fidelity failed to meet its obligations therein. The amount and nature of the deposits made in each of the depositary states are summarized in the opinion of the Circuit Court of Appeals (R. 241-242). These laws will be dealt with in more detail in the briefs of the several respondents.

8. Fidelity and the S E C

After the establishment of the Securities and Exchange Commission in 1934 Fidelity's affairs began to receive attention from a new quarter. The Securities Act of 1933 (15 U. S. C. A., sec. 77a to 77aa) required the registration of securities sold in interstate commerce under certain terms and conditions but contained an exemption for "any insurance or endowment policy or annuity contract or optional annuity contract, issued by a corporation subject to the supervision of the insurance commissioner, bank commissioner or any agency or officer performing like functions, of any state or territory of the United States or the District of Columbia." (Sec. (3) (8), Securities Act of 1933 (15 U. S. C. A., sec. 77c (a) (8)).

Fidelity maintained that its contracts were exempt from registration under this clause of the Securities Act (R. 859) although in 1939 it decided to register with the Securities and Exchange Commission (R. 860). However, although a registration statement was prepared, this was never carried out (R. 860-861). As has been shown, the Securities and Exchange Commission made a detailed investigation of Fidelity's business and the business of the two other chief companies selling similar contracts by virtue of sec. 30 of the Public Utilities Holding Company Act of 1935, its report to Congress comprising Ex. 6 in the record herein.

While Fidelity had maintained it was exempt from registration under the Securities Act of 1933, it was subject to the provisions of sec. 17 (15 U. S. C. A., sec. 77q) of that law, relating to fraudulent sale of securities in interstate commerce or by use of the mails.

On December 14, 1938 the Securities and Exchange Commission filed its bill for an injunction against Fidelity in the United States District Court for the Eastern District of Michigan, Southern Division, alleging that Fidelity was engaged in acts and practices which constituted violations of the fraud provisions of the Securities Act of 1933, sec. 17 (a).

On December 22, 1938 Fidelity filed its answer denying generally the allegations of the bill and on the same day consented to the entry of a decree enjoining it from engaging in the acts specified in the complaint. The bill of complaint and other proceedings and judgment therein are found at pp. 197-258 of Ex. 6 herein. This action on the part of the Securities and Exchange Commission received widespread publicity and resulted in contracts being presented for cash surrender to the extent of $9,000,000 (Ex. 21, R. 398). The sale of contracts was completely suspended during and for a period of time after those proceedings (R. 927).

In September of 1938 the peak volume of sales had been reached, contracts having a face amount of $5,600,000 being sold in that month (R. 926). Sales had been stepped up tremendously in the late 1930s. In round figures the total "face amount" sold in 1935 was $16,000,000; in 1936, $25,000,000; in 1937, $40,000,000 and in 1938, $52,000,000 (R. 926). In November of 1938 the volume was $4,700,000 and in December, when the SEC proceedings took place, $3,000,000 and in January and February, 1939 there was no volume

whatever (R. 927). After the SEC suit the highest volume reached was $1,500,000 in August, 1939 (R. 927), and sales were never again built to a point where the company could operate profitably on its then basis of operations (R. 934-935). During 1940 the monthly volume in each of ten months of that year was below $1,000,000 (R. 927).

Carroll D. Evans, who was director of agencies from 1935 to 1940, stated that when he took over the general sales management it was deemed necessary to sell a face amount of 2½ million dollars per month so that the income would meet the outgo (R. 922). Later the objective of $5,000,000 was set as a basis for profitable operations (R. 923). As a result of the SEC proceedings most of the states suspended Fidelity's licenses in 1938 or early in 1939 (R. 393).

On August 22, 1940 the Federal "Investment Company Act of 1940" was approved by the President after its passage by Congress upon the recommendation of the Securities and Exchange Commission after the completion of its report, a part of which comprises Ex. 6. The Investment Company Act became effective January 1, 1941 (insofar as it would affect Fidelity) and set up requirements to be met by companies selling face amount certificates which were utterly impossible for Fidelity to meet (R. 404, 630-631, 866, 946).

Thomas B. Foulk, who held the position of director and general attorney for the company during a period of from seven to nine years, and who had also been vice-president, stated that it was his opinion that under the Investment Company Act of 1940 Fidelity's business was through entirely and that he "just felt that we never could make the grade" (R. 946) and that after reading and

studying the Investment Company Act of 1940 he felt that "Fidelity could not continue and could not live" (R. 946). He said that Fidelity then turned to the idea of becoming a life insurance company as a means of continuing its existence (R. 946).

9. The various "funds" as shown by Fidelity's books

As we have shown, Fidelity sold various "series" of contracts from time to time during the years of its existence. In these contracts there were provisions substantially alike which provided that the Association should "create and maintain a reserve fund" for the discharge of its liability upon the particular series of contracts which contained the reserve fund provision. The reserve fund provisions are set forth in paragraph 1 of the various series of contracts (Exs. 1 to 5, inclusive). The earlier contracts, such as the "Special Income Contract" (Ex. 1) did not contain provisions as to the rate at which the reserve was to be improved. The later contracts (Exs. 2, 3, 4 and 5) provided that the reserve was to be created by placing therein a sum which, when improved, at an arbitrary reserve improvement rate, in some cases 4% and in other cases 4½%, would produce a sum sufficient to pay out the contracts in the particular series (R. 776-777).

In paragraph 1 of each of the contracts it was uniformly provided that the reserve fund appertaining thereto which the company contracted to maintain "shall be invested in approved securities and deposited in trust as required by the laws of the state of West Virginia" (Exs. 1 to 5, inclusive). The securities which the company purchased with payments received from contract holders were deposited with the state of West Virginia and with

state authorities elsewhere to comply with the laws of the particular states, but no attempt was made to designate which particular funds the securities came from in forwarding the securities to the various states, nor did the states themselves make any such allocation (Op. Dist. Ct., R. 181; R. 586-587; 634-635; 645-652; 663-667; 760-761). And see Ex. 27 (App. 76).

Prior to December 31, 1938 the cash payments received from the purchasers of various of the contract "series" were commingled in one bank account (Op. Dist. Ct., R. 180). This was changed after the SEC investigation. The securities on deposit with the states were at all times regarded both by the debtor, by the state laws and by the state authorities as securing all obligations to contract holders of the particular state where each deposit was made. The reports made to the states of total liabilities did not show such liabilities by "funds" (Ex. 78, R. 756).

The state deposits were established and the bulk of the securities presently therein was placed therein prior to December, 1938 when the SEC suit was brought. After the SEC suit the sales value was only a fraction of what it had been (*ante*, pp. 24-25), and the suit resulted in contracts being surrendered to the extent of $9,000,000 (*ante*, p. 24), all of which reduced the amount required to be kept on deposit. As shown by Ex. 80 (R. 757), the cash liability to contract holders on December 31, 1937 was over $28,000,000 and reserve liability over $30,000,000, as compared to cash liability of $23,000,000 and reserve liability of $24,000,000 on April 10, 1941. Thus, the deposits were established

without regard to the various "funds" to which the SEC directed attention at the time of its suits.

Except for the state deposits, the contracts were otherwise unsecured. As said in the SEC report (p. 1 of Ex. 6):

> "Irrespective of their designation, these certificates are in essence, simply unsecured obligations of the companies which issue them to pay a specified sum (called the face amount or maturity value or amount), provided the purchaser, promptly, and without any delinquency, makes all of the payments required by these contracts or certificates."

In a footnote in the report (p. 1, Ex. 6) it is then explained that some states require deposits and reference is made to a later discussion of these deposits in the report. See also p. 32 of "Part One" of Report of Securities and Exchange Commission pursuant to Section 30 of The Public Utility Holding Company Act of 1935, where it is said:

> "The certificate holder is not a stockholder of the corporation, which is private in nature, nor does he ordinarily have any interest in or lien upon any of the specific property or assets of the corporation. He assumes, in relation to the company issuing the certificates, the status of a general creditor, not unlike the holder of an unsecured promissory note or debenture of the company."

After the searching inquiry made by the SEC and in order to comply with the injunction decree and the Securities Act of 1933 it was necessary that the situation be fully explained to prospective purchasers of contracts (R. 764-765). Accordingly, in new prospectuses issued thereafter relative to the Series B contracts (p. 11 of Ex. 85, R.

766), a footnote to the balance sheet of the Series B fund stated:

> "The securities deposited with state authorities are subject to the requirements of the states with respect to all the contract funds of Fidelity Investment Association and are not necessarily held for the sole benefit of the holders of these particular contracts. In this connection reference is made to the foreword in this report."

The foreword to the financial statements in the prospectuses stated:

> "State laws with reference to deposits are not uniform. The laws of the states in which deposits against contract liability are required do not provide the mechanics for the segregation of portfolio securities of a particular contract fund against appropriate liabilities in the states of that fund, but merely provide for the deposit of a total amount of securities equal, in some cases, to the total contract liabilities, and in others, to a specified amount. In some states contracts were sold before any law requiring deposits was passed. For such contracts the deposits were made in West Virginia. The corporation recently adopted the policy of depositing portfolio securities belonging to one fund against liabilities of that fund alone, so far as state law permits, but it has been impossible to effect a transfer between various state authorities of securities heretofore deposited so that securities of funds for contracts heretofore issued will be deposited only against liabilities of that fund, although all securities are earmarked and segregated on the Association's books." (Ex. 85, R. 766)

See also Exs. 86 and 87 (R. 766). These statements were placed in the booklets after consultation with representatives of the SEC (R. 1152-1153).

In meeting obligations on maturing contracts, funds and securities were transferred and removed from one fund to another at will to meet the demands on any particular fund (R. 383, 388). The company also pursued a policy of issuing its preferred stock to matured contract holders in lieu of paying them out in cash (R. 390).

10. Previous efforts to recapitalize

As early as 1920 an effort was made to declare Fidelity bankrupt and a group was formed to buy out dissatisfied stockholders (R. 418). And we have seen that in 1933 its liabilities were in excess of its assets at market value in the amount of $7,000,000. Prior to 1936 the question of the depletion of the securities portfolio and the reserves had arisen and there was talk about trying to get new capital and how the company might be recapitalized (R. 1136) and reorganized (R. 425). From 1938 and continuously up to the time business was suspended constant efforts were made to get new capital. Arthur B. Koontz, one of the directors who had considerable acquaintance in the financial world, at the request of Fidelity's officers, besought many firms in the investment banking field to examine Fidelity's affairs with a view to refinancing. Negotiations were had with banking groups in Philadelphia (R. 1137), investment bankers in New York (R. 1137-1138) and a life insurance company (R. 1138). The Atlas Corporation, headed by Floyd Odlum, which company and its head were prominent in the investment banking field, worked on the project for some weeks but this too failed

(R. 1140). The Chicago Corporation of Chicago, which had also been asked to refinance Investors' Syndicate (a company engaged in the same type of business as that of Fidelity) went into the matter thoroughly but decided that it did not want to go into it (R. 1141). Extensive negotiations were had with the Morris Plan Bank of New York and with Mr. Arthur Morris, the head of that institution, who was familiar with Fidelity's business, but nothing came of this (R. 1141). Attempts were made to interest the Cleveland brokerage firm of Otis & Company (R. 1141). Some of the leading business men of Wheeling had a meeting and a plan was laid before them, but they evinced no interest in it (R. 1141-1142). Negotiations with Pell & Co. of New York foundered because among other reasons "they wondered whether or not a company operating in this field might be successful in the future" (R. 1139). In January, 1939, several weeks after the Securities and Exchange Commission's injunction suit in Detroit, efforts were made to place the company in a federal equity receivership. This litigation comprises the cases of *McCammon v. Fidelity Investment Association*, 26 F. Supp. 117 (N. D. W. Va., 1939) and *Hutchinson v. Fidelity Investment Association*, 106 F. (2d) 431 (CCA 4th, 1939).

In August of 1940 Allen G. Messick of Chicago was brought into the company at the instance of F. P. Pulfer (R. 525). Messick was an old school friend of Pulfer, and Pulfer had discussed the plight of Fidelity with him at a luncheon meeting in Chicago (R. 526). Messick interested one Rosset in Fidelity and Rosset and Messick entered into a contract with Fidelity whereby they were, on certain terms and conditions, to provide the sum of $500,000 so that Fidelity might continue its business (R. 1142). In

connection with this contract a voting trust of Fidelity's stock was created with John Marshall, Sr., as voting trustee. Although Marshall became voting trustee of Fidelity's stock, the money which Messick was to procure was not forthcoming and it was never produced. It is not quite clear why the plan fell through (R. 1143). Mr. Pulfer stated it was because it was found the money was to come from a Mr. Green in Chicago, who did not bear a good reputation and was later indicted by reason of some stock transactions (R. 526). Rosset brought suit against Messick and Fidelity in Chicago, charging breach of contract (R. 1143). Messick was elected to the Board of Directors in August, 1940, and became chairman of the Board in September, 1940, at a salary of $1,000 per month (R. 540). He received the salary for three months but it was cut off at the urgent request of Auditor Sims (R. 445-446). Auditor Sims did not know whether Messick had a real plan or whether it was a pretended plan, "a device to get inside" (R. 446). He felt that Messick "did not come to fetch the money, but he came to get the money" (R. 476).

11. The institution of the West Virginia state court proceedings

On March 25, 1941 Auditor Sims of West Virginia had written a letter (Ex. 94) to Arthur B. Koontz, one of the counsel for the company, advising that he contemplated instituting proceedings in the Circuit Court for Kanawha County, West Virginia (R. 1127). Mr. Sims had made very strong suggestions to the company earlier in the year that court proceedings would be necessary with respect to Fidelity's affairs (R. 1183). The situation was discussed with the officers of the company and with Mr. John Marshall, Sr., its chief counsel, and with Mr. Foulk, its gen-

eral attorney (R. 1183-1184). The company had had discussions with representatives of the SEC as to the type of court proceedings which would be best suited to the situation (R. 1184-1185). Both state and federal proceedings were discussed with varying opinions being expressed, and several members of the SEC staff advised the company that they did not wish to be put in the position of advising the company what the forum was to be (R. 1186). The possibility of federal reorganization proceedings was explored (R. 1187). It was finally determined that the best plan would be to go along with the West Virginia state court proceedings instituted by Auditor Sims (R. 1187-1188). On April 4, 1941 Auditor Sims ordered Fidelity to "freeze" its business, and thereafter Auditor Sims, acting through the Attorney General of West Virginia, instituted the proceedings in the Circuit Court for Kanawha County. The bill of complaint in that action comprises Ex. 21 (R. 398). On April 7, 1941 Fidelity's Board of Directors, upon motion of John Marshall, Sr., passed an unanimous resolution authorizing the law firm of Koontz and Koontz to represent it in the suit instituted in West Virginia by Auditor Sims (R. 1156-1157). Fidelity entered its appearance in the West Virginia proceedings but interposed no answer or objection thereto (R. 1192). Auditor Sims sent a copy of the bill of complaint in the West Virginia proceedings (Ex. 21, R. 308) to the various state authorities. Auditor Sims had also telegraphed the various state authorities asking that they institute proceedings to protect the assets in their respective states (R. 508).

In the West Virginia suit two receivers were appointed, being Ross B. Thomas and H. Isaiah Smith, and these receivers took certain assets into their hands, consisting of

cash in banks and undeposited securities of the value of some $500,000 (R. 819). The West Virginia state court receivers did not take over the assets on deposit with the State of West Virginia, which still remain with the State of West Virginia in the custody of the State Treasurer subject to the control of the Auditor (R. 819). The receiver Ross B. Thomas was an associate of the firm of Koontz and Koontz, and H. Isaiah Smith was formerly Budget Director of the State of West Virginia. After the commencement of the federal proceedings the federal trustee appointed H. Isaiah Smith to act in a managerial capacity in charge of the affairs of Fidelity (R. 477).

12. The institution of the other state court proceedings

Upon the company's suspending payment of its obligations and upon the institution of the West Virginia proceedings other state authorities took action.

Wisconsin

On April 14, 1941 proceedings were instituted by the Banking Commission of Wisconsin, under statutes providing for liquidation of foreign building and loan associations in that state. Notice of these proceedings was duly given to the officers of Fidelity and Fidelity was represented by its Wisconsin attorney. Fidelity did not oppose the proceedings in Wisconsin. Title to the Wisconsin assets of Fidelity, including the securities deposited with the State Treasurer in the amount of some $2,600,000, was vested in the Banking Commission of Wisconsin by order of the Circuit Court for Dane County, Wisconsin. The Banking Commission of Wisconsin proceeded to administer the affairs of Fidelity and prior to the institution of the Chapter X proceedings had

received proofs of claim from substantially all of the Wisconsin contract holders. These number about 12,000, of which approximately 6000 are "active." On May 27, 1941 securities comprising the approximate value of $1,259,000 of the Wisconsin deposit were liquidated and sold by the Banking Commission of Wisconsin, and these funds are presently held for distribution to Wisconsin contract holders. Ex. 120 (R. 3803 (original)) comprises a certified copy of the proceedings in Wisconsin. The Banking Commission of Wisconsin, through the Attorney General of Wisconsin, intervened in these proceedings and filed its answer controverting the allegations of the debtor's petition and is one of the respondents herein.

Iowa

The Iowa proceedings were instituted in the District Court in and for Polk County, Iowa, whereby Charles R. Fischer, Commissioner of Insurance of the State of Iowa, who had jurisdiction over Fidelity there, was appointed receiver. All of the securities comprising the Iowa deposit have been sold and the funds are presently held for distribution to contract holders. The proceedings in the Iowa state court are found in Ex. 121 (R. 3803 (original)) herein. The Commissioner of Insurance of Iowa intervened in these proceedings and filed an answer controverting the allegations of the debtor's petition and is one of the respondents herein.

Ohio

In Ohio, shortly after the West Virginia proceedings, a receivership action was instituted in the Common Pleas Court of Franklin County by John A. Lloyd, Superintend-

ent of Insurance of Ohio, through the office of the Attorney General of Ohio, for the purpose of taking possession of and protecting some $10,000 in undeposited assets in Ohio (R. 817).

The securities comprising the Ohio deposit were on deposit with the Treasurer of State of Ohio. This deposit is subject to liquidation under specific Ohio laws with reference to liquidation of deposits of insurance companies and bond investment companies (R. 817). The Treasurer of State of Ohio filed a motion to intervene in these proceedings, through the Attorney General of Ohio, which was granted, and filed an answer controverting the allegations of debtor's petition herein. This answer was withdrawn upon the entry of an order herein by the District Court on October 29, 1941, providing that the securities on deposit with the Treasurer of State of Ohio should remain there until such time as a reorganization plan might be adopted and approved in these proceedings, but without prejudice to Ohio's status as an intervener herein.

Illinois

In Illinois the Secretary of State with whom the Illinois deposit was made (although actual custody was with the State Treasurer) instituted a proceeding in the Circuit Court of Sangamon County, Illinois, for the appointment of a receiver for the preservation and maintenance of the securities on deposit in Illinois. This was in accordance with sec. 6 (a) of the Illinois Securities Act as amended providing for the liquidation of the securities on deposit in Illinois in the event of insolvency. These matters are set forth in the petition for leave to intervene filed in these proceedings by the Attorney General of the State of Illinois.

The Attorney General of Illinois filed an answer controverting debtor's petition on behalf of the State Treasurer and Secretary of State of Illinois. This answer was withdrawn upon the entry of an order herein by the District Court on October 4, 1941 providing that the securities on deposit in Illinois should remain there until such time as a reorganization plan might be adopted and approved in these proceedings.

Tennessee

In Tennessee certain contract holders on April 21, 1941 filed a bill in the Chancery Court in Davidson County, Tennessee, for the benefit of themselves and all other holders of contracts sold in Tennessee to enforce a lien on the Tennessee deposit which was made with the State Treasurer of Tennessee. These Tennessee contract holders intervened in these proceedings and filed an answer controverting the allegations of debtor's petition and are respondents herein.

Missouri

In Missouri a receiver was appointed in a suit commenced by the Attorney General of Missouri at the request of the Commissioner of Securities in the Circuit Court of Cole County. The Missouri receiver filed an answer controverting the allegations of debtor's petition herein and is one of the respondents herein.

Maryland

In the State of Maryland the affairs of Fidelity and the deposit are under the jurisdiction of the Insurance Commissioner of Maryland, who appeared in these pro-

ceedings and filed a motion to vacate certain orders of the District Court ordering the securities on deposit in Maryland to be turned over to the federal trustee. The Insurance Commissioner of Maryland is one of the respondents herein.

Kansas

The Securities Commissioner of the State of Kansas also entered an appearance in the proceedings through counsel.

No state holding a deposit complied with the turn-over portion of the orders of the District Court entered June 6 and June 10, 1941. The turn-over portion of such orders was rescinded by order of the District Court dated August 9, 1941. Since the filing of the federal petition the various state court proceedings have been held in abeyance except that under the order of the Circuit Court of Appeals for a stay of mandate the various state authorities have been permitted to send out proofs of claim to their contract holders.

More detailed reference to the proceedings which have transpired in the various states where Fidelity maintained a deposit or was otherwise regulated will be found in the briefs of the several respondents herein.

13. The institution of the federal proceedings

The decision to file the petition under Chapter X seems to coincide with the appearance on the scene of James R. Fleming, an attorney of Fort Wayne, Indiana, who was brought into the picture by Allen G. Messick, the most recent chairman of the Board, who was a close friend of Mr. Fleming (R. 1158-1159). John Marshall, Sr., who

prior to the appearance of Messick seemed to be the dominant figure in the company, appears to have come to rely upon Messick and Fleming. After the institution of the West Virginia proceedings Mr. Koontz discussed matters affecting the company with Mr. Marshall, and while Mr. Marshall did not express any dissatisfaction whatever with the course of the West Virginia proceedings, he told Mr. Koontz there were some people who thought the proceedings should be in federal court, and it finally developed that it was Fleming who had advised him in this regard (R. 1158-1159). Mr. Fleming conferred with Mr. Koontz and stated that he represented some interests in Fort Wayne, Indiana who might be interested in putting money into the company (R. 1160). He asked Mr. Koontz to prepare a plan of reorganization so he could indicate to his associates that there was some chance of rehabilitating the company, but Mr. Koontz stated that he could not do this in such a short time (R. 1161). Exhibit 115 (R. 3763 (original)), a letter dated November 25, 1940 addressed by John Marshall, Sr. to Arthur Koontz, would indicate that one of the reasons Mr. Marshall favored Mr. Messick was that he thought Messick could get money for the company and also that Messick would provide a place in the company for his son, John Marshall, Jr.

The filing of the petition under Chapter X was authorized by a directors' meeting held in Pittsburgh, Pennsylvania on June 3, 1941. There were only six directors present and seven were required for a quorum, so Mr. Fleming was elected as a member of the Board to make a quorum and resigned at the end of the meeting (R. 688-689). A. L. King, one of the directors, refused to vote for the filing of the federal petition because he felt that the state court receivers

had not had time to submit a plan in state court (R. 689-690). The District Court in its opinion held that this was not a legal meeting (R. 189-190). The petition under Chapter X was, however, filed on June 6, 1941.

On September 17, 1941, during the course of the hearing on the controversial answers to the debtor's petition, another meeting of the Board of Directors was held for the purpose of ratifying the filing of the petition (Ex. 92, R. 2205 (original)). Still later during the course of the hearing and on October 3, 1941 a stockholders' and directors' meeting was held to again ratify the filing of the petition (Exs. 98, 99, R. 959).

On June 7, 1941 the District Court entered an order authorizing the federal trustee to employ Mr. Fleming and Mr. Messick "for special services." This order was revoked by a later order dated August 1, 1941. Mr. Fleming and Mr. Messick conferred with the Banking Commission of Wisconsin on June 12 and stated that they had been authorized by the federal trustee to contact the various states to ascertain their attitude as to the deposits (R. 1054). Mr. Fleming stated to a meeting of state officials in Chicago on June 13 that he and Mr. Messick had been retained by the trustee to work out a reorganization plan (R. 848-849). Mr. Fleming represented the debtor at the commencement of the hearings on the controversial answers to the petition but withdrew during the course of the trial and was replaced by Mr. John Ray on September 17, 1941 (R. 662). There has been no indication whatever during the course of these proceedings that Mr. Fleming's group or anyone else would furnish any new capital for the debtor.

14. The obtaining of the life insurance charter and licenses

We have previously related that on December 31, 1940 the debtor amended its charter so as to become a life insurance company. Its sole charter purpose after that date was as follows:

> "To issue insurance upon the lives of persons and every insurance appertaining thereto and connected therewith, and to grant, purchase and dispose of annuities."

The change of charter was approved by the Insurance Commissioner and by the Secretary of State of West Virginia. The Insurance Commissioner also issued to the company a license to do business as a life insurance company on December 31, 1940, which expired March 31, 1941. The company applied for a renewal of such license and the Insurance Commissioner renewed it on April 1, 1941, to expire on March 31, 1942. All this is set forth in Ex. 24 (R. 437), the certificate of the Insurance Commissioner of West Virginia, found at page 76-79 of the Appendix to this brief. During the argument on the appeal in the Circuit Court of Appeals the debtor disputed the fact that the license as an insurance company was renewed on April 1, 1941, and at the request of the court the debtor and the respondents signed a stipulation (printed below) at the bar of the court to the effect that the debtor had applied for a renewal of the license shortly before April 1, 1941 and that this license was issued, but that on June 6, 1941 the license was not in possession of the company but was in possession of the Auditor of the State of West Virginia, and that prior to June 6, 1941 the check sent in payment for this license had been returned, and that the company was not operat-

ing under said license at the time the federal petition for reorganization was filed. Since Auditor Sims issued his "freeze" order to the company on April 4, 1941 and receivers were appointed on April 10, 1941, we may assume that the fees for the license for the year 1941-1942 were returned for the reason that the company was in effect out of business shortly after the issuance of the renewal license. The fees for the salesmen's licenses were also refunded, although the record does not show when (R. 462).

All through the trial in the District Court the debtor contended that it at no time issued any life insurance contracts under its charter and license as a life insurance company, and the District Court so found, and its opinion that the debtor was not a life insurance company was predicated upon such facts. However, it was subsequently discovered that the debtor had in fact issued many thousands of life insurance contracts by virtue of certain insurance "riders" under which Fidelity had assumed the life insurance provided for in the Series B contracts, which it had issued. These facts were brought to the attention of the Circuit Court of Appeals by a motion made by the West Virginia respondents, and at the request of that court the debtor, the Securities and Exchange Commission and these respondents entered into the following stipulation (R. 237-238):

> "Counsel admit at the Bar of the Court that the license applied for shortly prior to April 1, 1941, was issued but was in possession of the Auditor of West Virginia on June 6, 1941, and that the check sent in payment therefor was returned without being cashed prior to June 6, 1941, and that the Company was not operating under said license at the time of the filing of these proceedings on June 6, 1941; and that the total

number of riders sent out on December 31, 1940, which were signed by contract holders and returned to the Company, was 9,802; and that the total number of Series B contracts with insurance clause on December 31, 1940, was 14,626.

(Signatures omitted)"

"Approved April 20, 1942. John J. Parker, Senior Circuit Judge."

The "riders" which were referred to in the stipulation and which were executed by Fidelity and 9,802 persons were in form as follows:

"FIDELITY ASSURANCE ASSOCIATION

"ASSUMPTION OF RISK AND RIDER ATTACHED TO AND A PART OF INCOME RESERVE CONTRACT SERIES 'B' NUMBER

"The Association, having so amended its charter as to authorize it to issue insurance upon the lives of persons and every insurance appertaining thereto and to grant and dispose of annuities, and to change its name to Fidelity Assurance Association, in consideration of the monthly payments, provided for in the above numbered contract hereby assumes and does itself hereby agree to fulfill and pay all the risks and obligations of the insurance policy and the insurance company mentioned in Section C of said contract.

"It is hereby agreed between the Association and the contract holder that this insurance agreement shall become and be a part of said contract and the original shall be attached thereto.

"Executed in duplicate at Wheeling, West Virginia this 31st day of December, 1940.

FIDELITY ASSURANCE ASSOCIATION

(Signed) F. S. Risley
President

(Signed) Glenn W. Stephens
Contract Owner.

34S-11190 L
GLENN W. STEPHENS,
1st CENTRAL BLDG.,
MADISON, WIS."

When these "riders" were sent to such persons for execution a letter from Fidelity accompanied them which read as follows:

"December 31, 1940

"Dear Contract-owner:

"It is with pleasure and confidence that we direct your attention to the change in our name and the widening of the scope of our business to that of issuing insurance on the lives of persons. In the future, the company will be known as Fidelity Assurance Association and will offer a complete line of life insurance policies of all types and classes, including life annuities.

"These changes enable us, as a qualified legal reserve life insurance company to assume the risks and obligations provided in Section 6 of your contract. As you know, this Section makes available to you insurance covering all monthly payments not yet made in event of your death. Such insurance protection has, in the past, been procured from a legal reserve life insurance company, but was subject to cancellation upon due notice, at any time. With the making of your

regular monthly payments and the Association assuming the insurance, this condition has been eliminated.

"By resolution of the Board of Directors and by the rider enclosed in duplicate, the Association assumes and itself agrees to fulfill and pay the risk and obligations of the insurance policy and of the insurance company mentioned in Section 6 of your contract. The original of the rider is to be signed and attached to your Income Reserve Contract, Series B and the other (the blue one) signed and returned to the Association in the enclosed envelope." (See Ex. 100, R. 2863 (original))

The issuance of these riders had been formally approved at a special meeting of directors held December 31, 1940, whereby it was resolved that in view of the fact that the company was qualified and admitted to transact a life insurance business, it did thereby assume and agree to fulfill and pay all of the risks and obligations of the insurance policy and the insurance company mentioned in Sec. 6 of the Series B contracts. At this meeting life insurance policy forms were adopted, a medical director was selected and conditions under which the company would issue life insurance policies of various denominations were formally set forth (p. 156 of Ex. 100, R. 2863 (original)).

In addition to the official chartering and licensing of Fidelity as a life insurance company by West Virginia, the state issued licenses to twenty life insurance salesmen upon application of the company, and approved a number of life insurance policies to be issued (Ex. 24, R. 437, App. 76-79).

At the time of the issuance of the life insurance charter and license Auditor Sims and Fidelity had made a "gentle-

men's agreement" to the effect that the company would not sell any insurance policies until he gave permission (R. 406). With respect to this agreement Auditor Sims testified, "Those licenses were actually issued but the company was told not to sell anything until they got right with our office. I did that for the purpose of—licensed them for the purpose of receiving installment payments on the outstanding contracts." (R. 438)

However, in addition to continuing to receive payments on its outstanding annuity contracts by virtue of its life insurance company charter and license, the company in fact also issued life insurance policies and assumed life insurance risks.

Upon the charter change being authorized Fidelity notified the various state authorities of this fact. It addressed a letter to the Banking Commission of Wisconsin under date of December 21, 1940 as follows:

> "At a very recent meeting of the Board of Directors of the Fidelity Investment Association, it was unanimously decided that this company should broaden its field of activities by entering the life insurance business. The amendments to our charter, enabling us to write life contracts, were unanimously approved by the stockholders at their meeting. Under these circumstances we will discontinue the sale of contracts under our registration with your department and respectfully request that such registration be terminated at December 31 without prejudice." (Ex. 93, R. 2444 (original))

15. The plan and purpose behind the new charter

The federal "Investment Company Act of 1940" was to become effective on January 1, 1941, and it became obvious to the officers of the company that it could not comply with the requirements of this law so as to be able to continue in the business of selling face amount certificates (R. 403-404, 630, 701, 946). The idea of converting Fidelity's business into that of a life insurance company had been discussed by officers and directors of the company "about five or six months prior to the actual change" (R. 879-880). It had been discussed with John Marshall, who at that time was general counsel, with Mr. Foulk, the general attorney, the firm of Koontz & Koontz and others (R. 880). According to Fred Risley, the most recent president of the company, the officers knew at the time of the passage of the Investment Company Act of 1940 (August, 1940) that something would have to be done to change the form of Fidelity's business (R. 880-881). At first the thought was to try to develop a new form of annuity contract but that idea was abandoned and the idea of forming a life insurance company was adopted (R. 881). The company engaged an attorney in Chicago, who was experienced in the life insurance field, to assist in preparing the life insurance policies, rate book and "all the paraphernalia that goes with a life insurance company" (R. 879). The officers of the company considered that its business was already very similar to that of a life insurance company (R. 529).

Since 1934 the company had been selling the Series B contracts exclusively and 75% of the contracts sold had the life insurance feature (R. 681). The authorities of the states of Ohio, Kentucky and Alabama had ruled that the Series B contracts with insurance could not be sold in those

states unless the company was qualified as a life insurance company (R. 315). For this reason the Series D contracts were issued and sold in these particular states (R. 315). A substantial amount of the holders of the older contract series had converted them into Series B with insurance (R. 335-336).

It seems to be conceded by the proponents of the petition and others who testified in these proceedings, that if Fidelity should ever do business again it must be as a life insurance company (Ex. 29, R. 489; R. 416, 451, 457, 631, 670, 932-933, 944-945, 1086-1087, 1131, 1214-1215). In connection with Fidelity's conversion into a life insurance company it was necessary that its outstanding liabilities should be reduced so that it might go ahead as a life insurance company (R. 1157). Many plans were proposed. As expressed by Mr. Foulk, the company's general attorney, "as an insurance company, if we could work into that, I felt that there was a possibility of placating our people and having them comfortably go along" (R. 944-945). In order to accomplish this purpose, Fidelity, through Allen Messick, retained Raymond Latta, an experienced life insurance actuary, in February, 1941, to work out plans to have the company's contract holders voluntarily reduce their claims (R. 1125-1126). Fidelity was going "to try to put our men out and ask the contract holders to cut down their claims or contracts and still go on through reorganization outside any court" (R. 1185). Latta, in collaboration with others in the company, prepared various plans with a view to applying the contract holders' equities "toward the life insurance annuity contract" upon a voluntary basis (R. 1069). Among other plans prepared were a so-called "graduated reorganization plan" (Ex. 111, R. 1075) and a so-

called "uniform reorganization plan" (Ex. 112, R. 1075). All plans so prepared involved a scaling down of contract holders' interests. Mr. Latta was retained by the federal trustee until September 15, 1941 (R. 1056), but no plan for adoption in the federal proceedings has ever been submitted.

The purpose of becoming a life insurance company is made clear by John Marshall's letter of November 25, 1940, to Arthur Koontz (Ex. 115, R. 3763 (original)). He stated:

> "I think, too, that the idea of changing to an insurance company is an excellent one. Particularly in recent years that has really been our business—selling a contract with insurance features. If we become as successful as we once were in the sale of contracts, with a reduced guarantee and more participation in the strictly insurance features, we ought to make money again. Of course, one of the distinct features is that we leave our ally, the Investor's Syndicate, and join a strong group where we will be one of many. Finally, we get away from the S. E. C., which I think will always be an annoyance even if that body is reformed."

We should point out here that under the Investment Company Act of 1940, 15 U. S. C. A., sec. 80a, an insurance company is not an "investment company" so as to be subject thereto. Sec. 3 (c) Investment Company Act of 1940, 15 U. S. C. A., sec. 80a-3 (c). In the Investment Company Act of 1940 an insurance company is defined as follows:

> "'Insurance company' means a company which is organized as an insurance company, whose primary and predominant business activity is the writing of insurance or the reinsuring of risks underwritten by insurance companies, and which is subject to supervision by the Insurance Commissioner or a similar offi-

cial or agency of a state * * *" Sec. 2 (a) (17) Investment Company Act of 1940, 15 U. S. C. A., sec. 80a-2 (a) (17).

Fidelity's whole point and purpose in effecting the charter change was to come within this language so as to be an insurance company subject to state regulation only.

As expressed by A. L. King, who had been a director, assistant treasurer, vice-president, comptroller and secretary for many years, "Well, with the amended S. E. C. statute—whatever you call it—coming into force on January 1, we knew previous to that time that we could not continue to sell our contracts as Fidelity Assurance—Investment Association after that date. We felt, in view of the fact that we had been selling an insured contract for a period of four or five years which appealed to the public, that we could convert our association into an insurance company and broaden our field of activity to include other types of insurance and make a specialty of the sale of an insured contract that would pass the requirements of the State Insurance Commissioner" (R. 701).

John Marshall stated that Mr. Latta was well qualified to assist the company because "he had been in reorganization matters and was acquainted with the same type of business that we were in and in the insurance business that we would go into" (R. 1005).

Howard E. Reed, "vice-president in charge of bank and public relations" and a director of Fidelity, stated that many life insurance companies sold annuity contracts and referred specifically to the Franklin Life Insurance Company as doing "a general life insurance business and they sell an annuity contract" (R. 736). Henry M. Steussy, formerly Wisconsin sales manager for Fidelity, who had later

become vice-president of the Franklin Life Insurance Company, stated that that company was selling a face amount certificate which "qualifies as an insurance policy" and "was reconstructed just as the Fidelity contract would have to be reconstructed if the Fidelity Assurance Association was going to operate as an insurance corporation" (R. 1016, 1024). Fidelity intended to do the same thing.

Fred Risley, Fidelity's president, agreed that "everything was attempted that could lawfully and reasonably be attempted to begin the company's operation as an insurance company" (R. 885).

C. Facts particularly affecting the interests of Wisconsin contract holders and the Banking Commission of Wisconsin.

Fidelity was licensed to sell its contracts in Wisconsin and sold the same there from June 26, 1930 to the close of 1940. It was licensed annually by the Banking Commission of Wisconsin under the statutes of Wisconsin appertaining to foreign building and loan associations. Sec. 216.01, Wis. Stats., provides that corporations soliciting payments in a lump sum or periodically or on the installment plan must, in order to transact business in the state, comply with all of the provisions of Chapter 215, Wis. Stats., required of foreign building and loan associations authorized to do business in Wisconsin. Fidelity's business came within this description and thus it was licensed under Chapter 215 relating to building and loan associations. Sec. 215.38 of Chapter 215 provided that no foreign building and loan association should transact business in Wisconsin unless it should

> "* * * have and keep on deposit with the state treasurer, in trust for the benefit and security of all its members in this state, five hundred thousand dollars to be held in trust as aforesaid until all shares of such association held by residents of this state shall be fully redeemed and paid off and until its contracts and obligations to persons and members residing in this state shall have been fully performed and discharged. * * *"

It was also provided that the securities comprising the deposit should first be approved by the Banking Commission under the same rules and regulations as govern the approval of securities of trust company banks. It was further provided that whenever the Banking Commission should find that the liability on contracts held by persons residing in Wisconsin exceeded ninety per cent of the deposit, the Banking Commission should require the deposit of additional securities. Its contracts were also subject to the Securities Law of Wisconsin, Chapter 189, Wis. Stats. The laws of Wisconsin, insofar as pertinent here, to which Fidelity was subject are printed at pages 1 to 20 of the Appendix hereto.

Fidelity deposited securities with the State Treasurer of Wisconsin under these provisions of law. As of April 10, 1941, according to Fidelity's figures, the "net reserve liability" on contracts held by Wisconsin residents was $2,408,301.57, while the market value of the securities on deposit there as of June 6, 1941 was $2,619,399.07 (Ex. 48, R. 1116 (original)). About half of the securities comprising the Wisconsin deposit were liquidated and sold in the proceedings had there prior to the filing of the petition for reorganization herein, which securities are included in the latter figure.

The Wisconsin sales were directed from Fidelity's Milwaukee office which was in charge of Mr. Henry Steussy, who testified in these proceedings. A sales force of 225 men was built up in Wisconsin and a volume of over one million dollars in face amount per month was reached (R. 1011). Wisconsin was one of the five states in which the company had its largest volume of sales (Ex. 48, R. 1116 (original)). The total number of contracts outstanding in Wisconsin is approximately 12,000, of which approximately 6,000 are "active" (Ex. 34, R. 515).

In the sale of the contracts in Wisconsin the law of Wisconsin was emphasized (R. 1048). In the sales material prepared at the home office and used in Wisconsin the greatest stress was laid upon the fact that the company was supervised by the Banking Commission of Wisconsin and had securities on deposit with the State Treasurer. Ex. 106 (R. 1034), a handsome brochure used in making sales in Wisconsin, containing pictures of the state capitol of Wisconsin and quoting "the exacting law of Wisconsin." illustrates the method in which sales were made on the basis of the Wisconsin law. A great number of the Wisconsin contract-holders have advised the Banking Commission of Wisconsin that they purchased their contracts by reason of the representations made to them as to the Wisconsin law, and that since the money was placed on deposit for their protection they feel it should be paid over to them. The Wisconsin contract holders are not in favor of the federal proceedings. See Ex. 114, R. 3546 (original), printed at pages 27-36 of the Appendix hereto.

Upon the company's ceasing payment of its obligations in Wisconsin, and on April 14, 1941, three days after the institution of the West Virginia state court proceedings by

the Auditor of West Virginia, the Banking Commission of Wisconsin took possession of the Wisconsin business and assets of Fidelity under the statutory proceeding provided by the laws of Wisconsin for the liquidation of building and loan associations, particularly sec. 215.33, Wis. Stats. (App. 8). These proceedings were instituted in the Circuit Court for Dane County, Wisconsin. Due notice to Fidelity and its officers, as provided by statutes, was given and Fidelity entered its appearance therein by counsel, but interposed no objection to the proceedings. A certified copy of the Wisconsin proceedings comprises Ex. 120 (R. 3803 (original)) of the record herein. The Attorney General of Wisconsin represents the Banking Commission in the Wisconsin proceedings under provisions of Wisconsin law providing therefor. By operation of law (sec. 215.33 (8), Wis. Stats., App. 15) and as provided by the order of April 14, 1941, of the Circuit Court for Dane County (App. 22-25), title to and possession of all of Fidelity's assets located in Wisconsin were vested in the Banking Commission of Wisconsin "to be administered by the Banking Commission of Wisconsin under the supervision and control of the Circuit Court for Dane County, Wisconsin, for the benefit and security of contract, bond or certificate holders, residents of this state * * *" (App. 22). The filing of the notice of taking possession also operated under sec. 215.33 (8), Wis. Stats., as a bar to any action against Fidelity or its assets in Wisconsin, and this was also provided for by the court order. Actual custody of the deposited securities remained with the State Treasurer of Wisconsin pending the proceedings (App. 23). Under date of May 16, 1941 the Circuit Court for Dane County ordered that the Banking Commission should proceed to give notice for the filing of claims

Substantially all of the Wisconsin contract holders duly filed their claims with the Banking Commission of Wisconsin (Ex. 114, R. 3546 (original)) prior to the filing of the federal petition. The actual contracts were filed with these claims.

On May 16, 1941 the Banking Commission having determined that certain of the securities comprising the Wisconsin deposit should be sold, the court ordered that securities should be sold up to the amount of $1,500,000.

On May 27, 1941 the Banking Commission sold certain of the Wisconsin deposited securities realizing the sum of $1,259,244.04 therefor. This sale was approved by the court on May 29, 1941, and the funds realized ordered to be deposited in banks selected by the Banking Commission (Ex. 120, R. 3803 (original)). This was in accordance with sec. 215.33 (6), Wis. Stats., providing for the deposit of funds arising out of the liquidation of delinquent building and loan associations and providing that such funds constitute preferred deposits. These funds are presently held ready for distribution to Wisconsin contract holders. A schedule of the securities sold in Wisconsin with the par value and price realized thereon is contained in Ex. 120, (R. 3803 (original)) and is printed at page 26 of the Appendix hereto.

On June 9, 1941 the Banking Commission was notified by telegram, signed by Central Trust Company, that the District Court for the Southern District of West Virginia had on June 6 approved a petition for reorganization of Fidelity, and that all persons holding property of the debtor should turn the same over to Central Trust Company. Subsequently, copies of the District Court's *ex parte* orders of June 6 and June 10 ordering that the Banking Commission

should turn over any assets in its possession to Central Trust Company and enjoining continuance of the state proceedings were mailed to the Banking Commission. The Banking Commission of Wisconsin did not comply with these purported orders insofar as they provided for a turnover of the deposited assets to the federal trustee. It has voluntarily held its proceedings in *status quo* pending the determination of the jurisdiction of the District Court for the Southern District of West Virginia.

D. Facts particularly affecting the interests of Iowa contract holders and the Commissioner of Insurance of Iowa

Fidelity Assurance Association, formerly known as Fidelity Investment Association, made application under the latter name to the state of Iowa through its Executive Council pursuant to the provisions of Chapter 392, 1927 Code of Iowa, for authority to sell its contracts in the state and said application was granted and a certificate of authority issued out of the office of Auditor of State on or about January 7, 1929. At the time of the issuance of certificate of authority the debtor corporation deposited with the Auditor of State of Iowa approved securities in the sum of $25,000 pursuant to the provisions of Chapter 392, 1927 Code of Iowa, said deposit being made for the specific purpose of guaranteeing to Iowa contract purchasers faithful performance of debtor corporation's obligations. Thereafter debtor corporation deposited additional securities in an amount at all times equal to its liabilities in this state in accordance with Iowa law. (See App. 37-40 for Chapter 392).

Thereafter on March 28, 1930 debtor corporation registered its investment contracts as an issuer-dealer pursuant to the provisions of Chapter 393, 1927 Code of Iowa (now Chapter 393.1, App. 41-43) and also filed its written consent without power of revocation that suits and actions might be commenced and maintained in the courts of this state by service of process or pleading authorized by law on the Secretary of the State of Iowa, as required by law. After 1936 debtor corporation's license and certificate of authority were not renewed and it was thus prohibited from carrying on its business as an issuer-dealer. In order that said debtor coporation might continue to collect and disburse on its outstanding contracts, although prohibited from selling new contracts, it filed application under date of December 17, 1937 with the Secretary of the State of Iowa for a permit to do business as a foreign corporation, pursuant to the terms of Chapter 386, 1935 Code of Iowa (App. 50-52), and with said application filed a resolution adopted by its Board of Directors designating a resident agent on whom service of original notice of civil suits might be served in the manner provided for in Section 3421, Chapter 386, 1935 Code of Iowa.

Debtor's "net cash liability" to Iowa contract holders is approximately $35,000 and debtor has deposited in Iowa bearer securities of the approximate par value of $42,000. These securities were deposited by the debtor in trust for the express purpose of guaranteeing 100% faithful performance on the part of debtor corporation, pursuant to the provisions of Chapter 392 of the Code of Iowa.

On April 11, 1941 debtor corporation was adjudged and decreed to be insolvent in the state of West Virginia. The debtor corporation had for some time occupied a pre-

carious position in the state of Iowa, and upon the receipt of this information Charles R. Fischer, Commissioner of Insurance, through the Attorney General for the state of Iowa, commenced an action in the District Court in and for Polk County, Iowa to wind up the affairs of debtor corporation pursuant to the provisions of Chapters 392 and 393.1, Code of Iowa 1939. An order was entered on April 16, 1941 by the District Court in and for Polk County, Iowa, prohibiting any business transactions on the part of said debtor corporation.

Shortly thereafter one Guy R. Shaw, an Iowa resident contract holder, filed his petition in the nature of a creditor's bill, stating his interest and the interests of others similarly situated, alleging the deposit of securities in trust with the state for benefit of contract holders and the insolvency of debtor corporation and praying that an order issue appointing Charles R. Fischer temporary receiver. On April 23, 1941 Charles R. Fischer answered and cross-petitioned to Guy R. Shaw's petition, admitting that title to securities vested in the state of Iowa for use and benefit of contract holders on dates of their deposit and praying that he be appointed temporary receiver. On April 24, 1941 an order issued appointing Charles R. Fischer temporary receiver and prescribing the notice to be given to the Iowa resident agent, the receivers in West Virginia and the officers of debtor corporation, and said notice was duly given setting the day of May 19, 1941 as the date for hearing upon the appointment of Charles R. Fischer as permanent receiver of debtor corporation.

On April 24, 1941, on motion of John M. Rankin, Attorney General for the State of Iowa, an order was entered consolidating the original cause commenced by the Attor-

ney General with the cause commenced by Guy R. Shaw, a contract holder.

On May 1, 1941, one E. G. Pullen, a resident contract holder in debtor corporation, petitioned for leave to intervene for himself and other Iowa contract holders similarly situated and alleging the deposit in trust by debtor corporation in the state of Iowa and alleging debtor's insolvency; on May 3, 1941 an order issued from the District Court in and for Polk County, Iowa granting leave to intervene and prescribing notice to be given to debtor corporation and to Charles R. Fischer, temporary receiver, which notice was duly given.

On May 19, 1941 a decree and order (App. 52-62) issued from the District Court in and for Polk County, appointing Charles R. Fischer, Commissioner of Insurance, as Permanent Receiver for debtor corporation for Iowa. The court found and decreed that title to assets on deposit pursuant to Chapter 392, Code of Iowa, vested in the state of Iowa on the dates they were deposited, and that said title thereto was now by decree vested in Charles R. Fischer as Permanent Receiver for said debtor corporation and ordered said receiver to proceed to wind up the affairs of debtor corporation in Iowa and prescribed notice to be given to the Iowa creditors of debtor corporation and provided for bond to be given as permanent receiver and the District Court retained jurisdiction over the receiver and assets for winding up purposes.

On May 20, 1941 Charles R. Fischer filed final report as receiver *pendente lite*, alleging he is now Permanent Receiver for debtor corporation and praying that he be dismissed and discharged as temporary receiver; on May 22, 1941 the District Court in and for Polk County, Iowa

entered an order dismissing and discharging Charles R. Fischer as temporary receiver of said debtor corporation, and on May 23, 1941, *et seq.*, Charles R. Fischer, Commissioner of Insurance and Permanent Receiver for debtor corporation, issued full and complete notice as prescribed in the order and decree dated May 19, 1941. A certified copy of the Iowa proceedings comprises Ex. 121 (R. 3803 (original)) herein.

The Commissioner of Insurance, as Permanent Receiver for debtor corporation, proceeded to administer the assets of the debtor corporation pursuant to the laws of Iowa up to the time the debtor's petition for reorganization was filed herein. The assets on deposits were not turned over to the federal trustee. The Iowa proceedings have voluntarily been held in *status quo* up to the present time. All of the securities comprising the Iowa deposit have been liquidated and sold and the cash proceeds remain with the Commissioner of Insurance for distribution to contract holders. Preparation is being made for the filing of proofs of claim in the Iowa proceedings.

PROPOSITIONS RELIED UPON IN THIS BRIEF AND THEIR DISPOSITION BY THE COURTS BELOW

1. The debtor and petitioner is an insurance corporation within the meaning of Section 4 of the Bankruptcy Act as amended (11 U. S. C. A., sec. 22), and as such, ineligible to reorganize under the provisions of Chapter X of the Bankruptcy Act, Act June 22, 1938, c. 575, 52 Stat. 883.

The District Court held that the debtor was not such an insurance corporation, while the Circuit Court of Appeals, reversing the District Court, held that it was.

2. The debtor's petition for reorganization was not filed in good faith within the meaning of Section 144 and subsecs. (3) and (4) of Section 146 of Chapter X (11 U. S. C. A., secs. 541, 546 (3) (4)).

The District Court held that the petition was filed in good faith within the meaning of the designated statutes. The Circuit Court of Appeals, reversing the ruling of the District Court, held that the petition was not filed in good faith within the meaning of Sections 144 and 146 (4). It made no finding as to whether dismissal was also required under Section 146 (3).

3. The public interest, under well settled equity principles applicable in Chapter X proceedings, required dismissal of the petition.

This contention was not ruled upon in either of the courts below.

ARGUMENT

I.

THE DEBTOR IS AN INSURANCE CORPORATION WITHIN THE MEANING OF SECTION 4 OF THE BANKRUPTCY ACT, AS AMENDED, AND AS SUCH INELIGIBLE TO REORGANIZE UNDER THE PROVISIONS OF CHAPTER X OF THE BANKRUPTCY ACT

A. Insurance corporations are excluded from reorganization proceedings under Chapter X of the Bankruptcy Act

Section 4 of the Bankruptcy Act, as amended, 11 U. S. C. A., sec. 22, reads in part as follows:

> "(a) Any person, except a municipal, railroad, insurance, or banking corporation, shall be entitled to the benefits of this title as a voluntary bankrupt.
>
> "(b) Any natural person, except a wage earner or farmer, and any moneyed, business, or commercial corporation, except a building and loan association, a municipal, railroad, insurance, or banking corporation, owing debts to the amount of $1,000 or over, may be adjudged an involuntary bankrupt upon default or an impartial trial, and shall be subject to the provisions and entitled to the benefits of this title."

Chapter X, Section 106 contains the following provision:

> "For the purposes of this chapter, unless inconsistent with the context—
>
> "• • •

"(3) 'corporation' shall mean a corporation, as defined in this title, which could be adjudged a bankrupt under this title, and any railroad corporation except a railroad corporation authorized to file a petition under section 205 of this title;"

11 U. S. C. A., sec. 506 (3).

The question is squarely presented as to whether the debtor is an insurance corporation and therefore precluded from instituting reorganization proceedings.

B. The debtor was chartered, licensed and engaged in business as an insurance corporation under the laws of West Virginia, the state of its incorporation

The debtor was originally organized as a brokerage company and in 1912 its charter was amended to enable it to engage in "the business of soliciting and receiving deposits and payments on any annuity contracts, certificates or annuity bonds." From 1912 to December 31, 1940 it operated under the provisions of Ch. 33, Art. 9, sec. 1 of the West Virginia Code, reading:

"No person, association or corporation shall engage in the business of soliciting or receiving deposits or payments on any annuity contract or certificate or annuity bond in fixed and stipulated installments, within this State, without first having obtained from the insurance commissioner a license to do business in this State: *Provided, however, That this article shall not be construed as applying to* * * * *insurance companies,* * * * *duly authorized to do business in this State,* * * *. Such license shall be issued for one year, or the fractional part of a year, * * * and the provisions of section twelve, article two of this chapter [which provide for expiration April 1 each year] shall apply to such license." (Emphasis supplied)

During this period the debtor operated under the name of Fidelity Investment Association. We made no claim in the court below[1] and make none here that Fidelity was an insurance corporation during that period of its operation. As suggested in the petitioners' brief, it could hardly be regarded as an insurance corporation when such corporations were excluded from the provisions of the statute pursuant to which it was licensed.

On December 31, 1940 by charter amendment Fidelity's name was changed to Fidelity Assurance Association and the following statement of corporate purpose was substituted for that under which it had been operating:

> "To issue insurance upon the lives of persons and every insurance appertaining thereto and connected therewith, and to grant, purchase and dispose of annuities."

A certified copy of the charter amendments and a certificate by the Insurance Commissioner of West Virginia setting out the steps that were taken in connection therewith may be found in Exhibit 24 which is printed at pp. 76 to 78 of the Appendix.

According to the Insurance Commissioner's certificate, application was made to him pursuant to the provisions of Ch. 33, Art. 2, sec. 3 of the West Virginia Code to approve the amendments. That section provides that the Secretary of State may not issue a certificate of incorporation to an insurance company until the Insurance Commissioner shall have approved the charter in writing. Exhibit 24 shows that the Insurance Commissioner approved the amended charter pursuant to sec. 3 and Fidelity's application, on

---

[1] An intimation to the contrary in petitioner's brief (p. 33) is unfounded.

December 31, 1940. The Secretary of State of West Virginia then issued a certificate of amendment (App. 78-79).

Exhibit 24 also discloses that following the amendment of its charter and on the same day, Fidelity applied to the Insurance Commissioner for a license to engage in the insurance business. A license was issued under the provisions of Ch. 33, Art. 2, sec. 6 to transact such a business in West Virginia. A certified copy of the license is included in Exhibit 24. That part of the exhibit is not printed in the Appendix, since we have had no copy of the document.

At the time the debtor was chartered and licensed as an insurance company and thereafter during all the times involved in these proceedings, the law of West Virginia contained the following provision:

> "Life insurance companies chartered by and doing business in this State, and empowered to make contracts contingent upon life, may grant and issue annuities, either in connection with or separate from contracts of insurance based upon life risks, and all such annuities heretofore issued by such companies shall be valid." (Ch. 33, Art. 3, sec. 7, West Virginia Code)

The license to the debtor to engage in business as an insurance company was issued pursuant to an informal understanding with the Insurance Commissioner that it would enter into no new contracts of any kind until he advised the company that it might do so. The Commissioner testified that he issued the license at the time in order that the debtor would have authority to receive payments under its outstanding contracts (R. 438).

Under its charter and license as a life insurance company the debtor carried on its annuity business by continuing to receive payments upon outstanding contracts, by paying out amounts due on outstanding contracts and

by managing its securities portfolio (R. 182). It does not appear that it attempted to write any further annuity contracts. The same cannot be said, however, with respect to insurance contracts.

At the hearing in the District Court those officials of the debtor who should have been in a position to know of its activities testified that it had issued no insurance policies after its incorporation and licensing as a life insurance company. After the case had been decided by the District Court and while the appeal to the Circuit Court of Appeals was pending, evidence was uncovered which established that the company had in fact entered into life insurance contracts. A motion was made in the Circuit Court of Appeals to remand the case for further testimony. The motion was considered at the same time that the case was argued in the Circuit Court of Appeals, and counsel for all parties stipulated at the bar of that court that certain riders were sent out by the company in December 31, 1940 to the holders of its Series B contracts with the insurance clause.[1] It was stipulated that 9,802 riders were executed by contract holders and returned to the company, and that the total number of outstanding contracts with the insurance clause as of that date was 14,626 (R. 237).

The riders to which this stipulation referred are set out in the statement of facts (*ante*, p. 43-44). We have also set out a letter which accompanied the riders. The letter in plain words advised each contract holder that the company had become authorized to engage in the insurance business; that it desired to assume the insurance provided for in his annuity contract; that it was enclosing a rider which it had executed and by virtue of which it would

[1]The nature of the insurance clause is discussed in the statement of facts, *ante*, p. 8-9.

assume the insurance when the rider had been executed and returned to it.

The debtor and the trustee in their brief do not unequivocally deny that by reason of the execution and return of these riders the company entered into 9,802 insurance contracts. They say, however, that the finding of the Circuit Court of Appeals that the contracts existed was made without "thorough consideration," and that they do not concede such contracts were created. They admit that by virtue of the riders, the company "would have assumed the insurance obligations * * *—when, if ever, * * * [it] could clear with the West Virginia State Auditor and get the right to issue insurance contracts" (Debtor's brief, p. 37).

It is preposterous to contend that any informal understanding with the Insurance Commissioner that it would not issue insurance contracts could invalidate such contracts issued by Fidelity under its unconditional license. There is no suggestion that any of the contract holders who entered into an insurance contract with Fidelity was advised of any such informal agreement. In fact, each holder was advised by the letter accompanying the rider that the company was ready, able and willing to enter into an insurance contract with him. We refuse to seriously consider the implied suggestion by the debtor and the trustee that no insurance agreements were effectuated with the 9,802 contract holders who executed and returned riders.

The brief of the Securities and Exchange Commission refers to Fidelity's insurance obligation as an "illegal gratuitous assumption of a liability" (SEC brief, p. 23). We are not advised in the brief of the respect in which these contracts were illegal; nor are we advised of the respect

in which they were gratuitous. As in the case of the debtor and the trustee, the Securities and Exchange Commission fails to offer anything resembling a valid argument to the effect that these executed insurance riders forming a part of Series B contracts, upon which contract holders continued to pay the amounts called for by the contracts, did not constitute insurance contracts, binding upon the company.

The insurance contracts entered into by the debtor were nonetheless so because it continued to cover its liability by continuing its group insurance policy with Lincoln National. As the Series B contracts with the insurance feature were originally written, the debtor agreed, for a stipulated portion of the payment due on the contract, to obtain insurance that would protect the estate of the contract holder against loss of the contract in the event of his death prior to contract maturity. The debtor carried out its obligations under such contracts by obtaining a group life insurance policy with Lincoln National Life covering such Series B contract holders. After Fidelity itself assumed the insurance risk provided for in these Series B contracts it continued to carry the group policy with the Lincoln National Life. So far as we are advised, any claim against Fidelity arising out of its insurance contract has been paid by Lincoln National Life.

The fact that Fidelity has continued to carry its group policy with Lincoln National, however, does not affect the validity of its own insurance contracts. Actually the practical result of its doing so has been that it has carried reinsurance to the extent of 100% of its own insurance obligation. Had Lincoln National become insolvent to a greater extent than is Fidelity, so that it would be to the interest

of a contract holder to assert a claim against Fidelity directly on his contract, no court would say that Fidelity had escaped its obligation by covering the contract holder through a group policy with Lincoln National. And if today coverage under the group policy with Lincoln National were to be cancelled as applied to those with whom Fidelity has contracted, there could be no question as to Fidelity's liability to those contract holders.

Summarizing the debtor's status as an insurance company under West Virginia law, it is established that it applied for incorporation as a life insurance company under the provisions of law particularly applicable to the incorporation of insurance companies; that it applied for and obtained an unconditional license to transact a life insurance business in West Virginia; that under its charter powers as a life insurance company and under West Virginia law it was empowered to deal in life insurance and in annuities; and that pursuant to its charter and its license it assumed liability on 9,802 life insurance policies and continued to carry on its annuity business except for the writing of new contracts. Debtor thus was chartered and licensed as a life insurance corporation by West Virginia and it transacted business in that state as such.[1]

Opposing briefs, both by the debtor, trustee and the Securities and Exchange Commission, attempt to gloss over Fidelity's status after its incorporation as a life insurance company by repeated statements that it was but a step

---

[1]No license was in effect at the time the debtor filed its petition. The license granted on December 31, 1940 expired on April 1, 1941. Application was made for a new license. The license was issued (App. 78), but the payment therefor was later refunded and the license returned. It does not appear as to when this was done except that it was done prior to the time the petition was filed (R. 237). Presumably the Commissioner felt obligated to return the money, since he ordered the company to cease business on April 4, 1941 and took it over under statutory receivership proceedings on April 11, 1941. While the difference is perhaps not material, the renewal license was not refused, as suggested in opposing briefs.

in an abortive "extra-judicial reorganization." They suggest that its incorporation, licensing and transaction of business as an insurance company was an effort to resuscitate the company as a paying business enterprise and that since the effort failed Fidelity cannot be regarded as having become a life insurance corporation. The suggestion implies that something necessary to constitute it a validly organized, licensed and operating insurance company remained uncompleted. Such an implication is contrary to the plain facts of the case, as we have already pointed out.

C. At the time insurance corporations were excluded from the Bankruptcy Act (1910), life insurance corporations were generally classified as such by reason of their charter powers to insure lives and to "grant, purchase and dispose of annuities"

We have seen that under the law of West Virginia, life insurance companies are those empowered to issue life insurance and to "grant and issue annuities." We have, moreover, seen that the sole corporate purpose of the debtor was

> "to issue insurance upon the lives of persons and every insurance appertaining thereto and connected therewith, and to grant, purchase and dispose of annuities."

The law of West Virginia in thus classifying debtor as an insurance corporation is the same as that which has existed in the majority of states of the United States for many years.

Insurance corporations were excluded from the Bankruptcy Act by Act June 25, 1910, c. 412, secs. 3 and 4, 36

Stat. 839. At that time twenty-eight states,[1] including the territories of Arizona and New Mexico, classified a life insurance company as a corporation formed for the purpose of insuring the lives of persons and "to grant, purchase and dispose of annuities." The statutory language varies in the several states but the substance is clearly as indicated. We have set out at pages 63-73 in the Appendix the statutory provisions of these twenty-eight states. A typical case is that of New Jersey, where the law provides as follows:

> "Ten or more persons may become a corporation for the purpose of making any of the following kinds of insurance to wit:
>
> "* * *
>
> "—Life.—III. Upon the lives or health of persons, and every insurance appertaining thereto, and to grant, purchase or dispose of annuities;"
>
> Compiled Statutes of New Jersey, (1709-1910) Vol. 2, p. 2838.

It will be noted that this statutory provision defining the purposes for which life insurance corporations may be organized is almost identical with the charter purpose of the debtor.

Twenty states did not in 1910 have statutory provisions such as those pointed out. Some of them defined life insurance corporations as companies issuing insurance on the lives of persons, without making mention of the power to issue any form of annuity contract. Others did not define

---

[1] Territory of Arizona, California, Colorado, Connecticut, Illinois, Indiana, Kansas, Kentucky, Louisiana, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Montana, New Jersey, Territory of New Mexico, New York, North Carolina, Ohio, Oklahoma, Oregon, Pennsylvania, Texas, Washington, West Virginia and Wisconsin.

the term. Of these twenty states, however, at least seven[1] have amended their statutes since 1910 to conform to the statutes of the twenty-eight states, to which reference has been made. The statutes of these states are set out in the Appendix at pages 73-75.

It is, of course, an undeniable fact that in the year 1910 there was no commonly accepted meaning attached to the term "life insurance corporation" except as such meaning was derived from the laws of the several states which provided for the incorporation and regulation of such corporations. This is true also today. The federal government did not in 1910, and does not now, assume to incorporate life insurance companies for the purpose of carrying on a general life insurance business. It is established, therefore, that the term "life insurance corporation," in the year 1910 and today, in common, ordinary usage and understanding implies a corporation organized to issue insurance upon the lives of persons and to "grant, purchase and dispose of annuities." Such companies are in many cases empowered also to engage in activities such as writing accident and health insurance. We are not concerned with such powers in this case, however.

---

[1] Arkansas, Idaho, Iowa, New Hampshire, Utah, Vermont, Wyoming.

D. The question as to whether debtor is an insurance corporation within the meaning of the Bankruptcy Act is to be determined either (1) by its classification under the law of West Virginia or (2) by its classification according to the accepted usage and understanding at the time of and since the enactment of the amendment of 1910 excluding insurance corporations from the Act. Under either test the debtor is an insurance corporation.

The adjudicated cases are not entirely consistent upon the test to be applied in determining whether a corporation falls within the classes excluded from the Bankruptcy Act by the provisions of sec. 4, 11 U. S. C. A., sec. 22. Five circuits, including the Fourth in the present case, hold that the question is to be determined by the classification of a corporation by the laws of the state of its creation, while one circuit holds that Congress intended to exclude such corporations as were generally recognized to be within the excepted classes at the time the Bankruptcy Law was amended to remove them from its operation. It is apparent that there could be no conflict in the two views, however, unless some state were to classify an excluded corporation upon the basis of charter powers other than those which are generally identified with such a corporation. We have found no case in which this has been true.

1. Authorities holding that classification by the state of incorporation is controlling

Perhaps the leading case holding to this view is *In re Union Guarantee & Mortgage Co.*, 75 F. (2d) 984, 985 (CCA 2d, 1935), where the court stated the principle in the following language:

"* * * The most natural inference is that Congress meant to leave to local winding up statutes the liquidation of such companies; that, since the states commonly kept supervision over them during their lives, it was reasonable that they should take charge on their demise.[1] * * * Now it is the powers conferred upon the company, not its activities, which are decisive. * * * So far as In re Supreme Lodge of Masons Annuity (D. C.) 286 F. 180, holds otherwise it cannot be accepted. If a state enacts that companies having powers of a prescribed kind must be regulated, that is of course authoritative; and, if in addition it classes the company as a bank or a railroad or an insurer, that too should be authoritative. Kansas v. Hayes, 62 F. (2d) 597 (C. C. A. 10); Security B. & L. Ass'n v. Spurlock, 65 F. (2d) 768 (C. C. A. 9). This is true, not because Congress was bound to yield in such cases, but because otherwise its apparent purpose to leave the winding up of such companies to the state would not be effected; for the will of the state is no clearer to supervise the company than to class it as it does. When Congress excepted not all companies affected with a public interest, but specified kinds of such company, presumably it intended the states to define the kinds."

---

[1]The court's inference was properly drawn. Mr. Jacob Weinstein, a member of the National Bankruptcy Conference, who assisted in the drafting of Ch. X and who appeared at the hearings before the House Committee on Judiciary to explain the bill, stated that such was the purpose of its framers. He said:

"We have a letter from Mr. E. R. Elliott, an attorney of St. Louis, Mo. Mr. Elliott suggests that insurance companies be brought within the scope of corporate reorganizations. The conference has thoroughly canvassed and considered that whole subject of persons amenable to reorganization proceedings, and they have decided that in the case of insurance companies and banking corporations and the like, they be not brought within the scope of the reorganization proceedings. The cases of these companies, which are now excluded from the act—the various States have set up, first, controlling agencies in the operation of the companies; and, secondly, when companies become embarrassed, the agencies, in order to take care of them and to liquidate them, when necessary, and it is the judgment of the conference that it would be much better to allow these companies to be liquidated or reorganized under local law, than to bring them in under the bankruptcy law * * *" (House Committee on Judiciary, Hearings on H. R. 6439, 75th Congress, 1937-38, p. 242)

Cases from other circuits so holding are:

Grand Lodge, Knights of Pythias v. McKee, 95 F. (2d) 474 (CCA 5th, 1938);

State of Kansas v. Hayes, 62 F. (2d) 597 (CCA 10th, 1932);

Security Building & Loan Ass'n v. Spurlock, 65 F. (2d) 768 (CCA 9th, 1933).

2. The view that a generally recognized rather than a local state classification is controlling

The highest authority that we have found supporting the view that local classification is not controlling is *Gamble v. Daniel*, 39 F. (2d) 447 (CCA 8th, 1930). There the question was whether a corporation organized under the laws of Nebraska was excluded from the Bankruptcy Act as a banking corporation. The court discussed the matter as follows:

"* * * We have no doubt that when Congress used the words 'banking corporations' it meant corporations which were authorized by the laws of their creation to do a banking business.

"* * * When Congress spoke of 'banking corporations' it spoke as of 1910. It used the words in no technical nor special sense, but as they were then ordinarily understood. As that time, the ordinary conception of a bank was of a business which was based primarily on the receipt of deposits (general or special), which deposits were used by the bank for loans, discounts, buying and selling commercial paper, and other business purposes. * * * Without attempting a full definition of these words used in this section of the Bankruptcy Act (as amended), this necessary element of deposits is stressed because it is important in this case.

"Having in mind the above construction of the words in the Bankruptcy Act, we turn to the statutes of Nebraska to ascertain the powers of this company. In such examination we are not bound by terminology, but are seeking to ascertain the actual powers granted. * * *." *Gamble v. Daniel*, 39 F. (2d) 447, 450-451.

The case of *In re Supreme Lodge of the Masons Annuity*, 286 F. 180 (N. D. Ga., 1923), also holds to this view.

3. Cases involving possible qualifications of the local state classification rule need not be considered

It is not necessary for the purposes of this case to consider whether the rule of *In re Union Guarantee & Mortgage Co.*, 75 F. (2d) 984 (CCA 2d, 1935) was modified by the Second Circuit Court of Appeals in the case of *In re Prudence Co.*, 79 F. (2d) 77 (CCA 2d, 1935).

It might be contended on the basis of the *Prudence* case that a state could not classify a corporation as a "railroad, insurance, or banking corporation" unless its charter purposes and the law under which it does business permit it to exercise some of the powers which have been commonly accepted as belonging to such corporations. But see *Empire Title & Guarantee Co. v. United States*, 101 F. (2d) 69 (CCA 2d, 1939). Neither is it necessary to consider other cases where it might likewise be contended that the rule of local state classification might be so limited.

Cf. Clemons v. Liberty Savings & Real Estate Corporation, 61 F. (2d) 448 (CCA 5th, 1932);

Woolsey v. Security Trust Co., 74 F. (2d) 334 (CCA 5th, 1934).

In the present case the debtor was classified as a life insurance corporation upon the basis of charter powers which are generally characteristic of life insurance corporations.

If a state were to enact that any corporation organized under its laws should be an insurance corporation, and if it were claimed that a corporation organized under its laws to operate a restaurant were an insurance corporation and excluded from the Bankruptcy Act, it might be contended with some force that the federal courts should refuse to follow the state classification. Such a case has not arisen to date, however, though many years have elapsed since these various types of corporations were excluded. Nor is it probable that the courts will be confronted with such a case. But if the time comes when states thus abuse the power that Congress has relinquished to them to reorganize and liquidate these particular classes of corporations, the Congress may, by a change of definitions or by removal of the exclusion clause altogether, adequately deal with the situation.

4. Debtor is an insurance corporation whether regard be had to its West Virginia classification or whether it be judged on the basis of a generally recognized classification

We have already pointed out that the debtor was organized as a life insurance corporation under the laws of West Virginia and that it was licensed and did business as such. If its status is to be determined upon the basis of its classification under the law of West Virginia, then it must necessarily be an insurance corporation.

If we turn from the matter of local classification and regard the debtor's status upon the basis of the general and

accepted meaning of the term "life insurance corporation" at the time such corporations were excluded from the Act in 1910 by Act June 25, 1910, c. 412, secs. 3 and 4, 36 Stat. 839, it is likewise established, as we have shown, that the debtor is an insurance corporation.

E. There is no merit to the contention that the debtor's status as an insurance corporation is to be determined by considering the nature of its predominant activity and that, as so determined, it is not an insurance corporation

The debtor, the trustee and the Securities and Exchange Commission have contended throughout this case that the debtor's status as an insurance corporation is to be determined by application of what those of us interested in the case have denominated the "activities doctrine." They wholly reject the rule that the status of a corporation is to be determined by its classification under the laws pursuant to which it was organized. They agree with the one Circuit Court of Appeals decision, *Gamble v. Daniel*, 39 F. (2d) 447 (CCA 8th, 1930); which rejects the local classification rule and adopts a rule of generally recognized classification. They disagree with the *Gamble* case, however, in that they contend a corporation's status should be determined by its predominant activity rather than its charter powers, whereas the *Gamble* case holds that classification by charter power is the proper rule. They thus stand without support for their doctrine from any Circuit Court of Appeals decision construing the exclusion clause of the Bankruptcy Act now under consideration. The proposition contended for by the petitioners and the Securities and Exchange Commission was accepted by the District Court and was thus stated in its decision:

"In deciding whether a corporation is to be classified as an insurance or banking corporation or a building and loan association within the meaning of the Bankruptcy Act, the court must first examine the provisions of its corporate charter. If the charter authorizes the company to engage in business in any of the excepted fields, and if the company in fact engages principally in a business which lies within that field, such a corporation must be treated as one excluded from the benefits of Chapter X. However, if its charter authorizes the corporation to engage in activities outside the excepted fields, and if all the business actually done by the corporation is outside those fields, then it must be treated as not being within any of the excluded classes. By this test Debtor must be classified as a corporation which is not an insurance corporation within the meaning of the exemption provisions of the Bankruptcy Act. * * *." (R. 189)

The court then distinguished "insurance annuities" (life annuities) from "investment annuities" (annuities for a term of years). It held that the only business conducted by the debtor under its charter and license as a life insurance company involved "investment annuities" and that it did not, therefore, transact an insurance business.[1] Accordingly, the court held that since transactions in investment annuities constituted the debtor's only business and since such annuities were not insurance, the debtor was not an insurance corporation.

It should be remarked, first of all, that the District Court erred in the distinction it attempted to draw between "insurance annuities" and "investment annuities." It is to be inferred from its decision that had Fidelity's activities

[1] The issuance of life insurance contracts was not known to the court. See discussion ante, p. 66.

after its incorporation as a life insurance company consisted of dealings with reference to life annuities, it would be regarded as a life insurance company. But no annuity contract, either for life or for a period of years, is an insurance contract.

Helvering v. LeGierse, 312 U. S. 531, 541-542, 85 L. ed. 996, 61 S. Ct. 646 (1941);

Old Colony Trust Co. v. Commissioner of Internal Rev., 102 F. (2d) 380 (CCA 1st, 1939);

Rishel v. Pacific Mut. Life Ins. Co. of California, 78 F. (2d) 881 (CCA 10th, 1935);

In re Walsh, 19 F. Supp. 567 (D. C. Minn., 1937);

Commonwealth v. Metropolitan Life Ins. Co., 254 Penn. 510, 98 A. 1072 (1916);

State v. Lucas, (Mo.) 153 S. W. (2d) 10 (1941);

Curtis v. New York Life Ins. Co., 217 Mass. 47, 104 N. E. 553 (1914);

People v. Knapp, 193 App. Div. 413, 184 N. Y. S. 345 (1920), affirmed 231 N. Y. 630, 132 N. E. 916 (1921);

Daniel v. Life Ins. Co. of Virginia, (Tex. Civ. App.) 102 S. W. (2d) 256 (1937);

State v. Equitable Life Assur. Soc., 68 N. D. 641, 282 N. W. 411 (1938);

Northwestern Mut. Life Ins. Co. v. Murphy, 223 Ia. 333, 271 N. W. 899 (1937);

State v. Ham, 54 Wyo. 148, 88 P. (2d) 484 (1939).

Life insurance corporations under their charter power to deal in annuities may issue such annuities for life, upon

the basis of mortality tables, or for a certain period without regard to mortality tables, as in the case of Fidelity's annuities.

Carroll v. Equitable Life Assur. Soc. of United States, 9 F. Supp. 223, 224 (D. C. Mo., 1934);

Daniel v. Life Ins. Co. of Virginia, (Tex. Civ. App.) 102 S. W. (2d) 256, 260 (1937).

And life insurance corporations conducting an annuity business under a life insurance charter to deal in life insurance and annuities and under a license to conduct a life insurance business are regarded as engaged in a life insurance business. As stated by the Supreme Court of Massachusetts:

> "And the conclusion is irresistible that if the petitioner had issued only contracts for the payment of annuities, it must be deemed to be a life insurance company. If so it would be accurately described as in 'the business of life insurance.' It is none the less so engaged because it also issues policies of life insurance. * * *." *Mut. Ben. Life Ins. Co. v. Commonwealth*, 227 Mass. 63, 116 N. E. 469, 470 (1917)

and by the Supreme Court of Iowa:

> * * * That these words 'business done in this state' were inclusive of the granting and selling of annuities was made definitely certain by legislative enactment prior to the year 1934. That is, the Legislature had identified the granting and selling of annuities as a part of the business permitted and anticipated to be done in this state by insurance companies in the enjoyment of their business licenses. Reference is to chapter 147 of the Acts of the Forty-fifth General Assembly, which

added to chapter 308 of the 1931 Code, section 8673-a, which provides that 'any life insurance company organized on the stock or mutual plan may grant and sell annuities. * * *.' *Northwestern Mut. Life Ins. Co. v. Murphy*, 223 Ia. 333, 271 N. W. 899, 902 (1937)

See also: *State v. Lucas*, 348 Mo. 286, 153 S. W. (2d) 10 (1941).

It must therefore be concluded that, even assuming the rule of law applied by the District Court to be applicable, it was misapplied in that if the annuity business done by Fidelity after its incorporation as a life insurance company constituted its predominant activity, the activity nevertheless was that of a life insurance company doing a life insurance business. The situation is comparable to the activity of the trust department of a banking corporation. Banking corporations authorized to conduct a trust business are nevertheless banking corporations, and the trust department cannot be considered apart from the corporation which conducts it and be regarded as something other than a banking business. *Sterling v. Tantum*, 5 Boyce (28 Del.) 409, 94 A. 176, 182.

An annuity business may be transacted by a corporation other than a life insurance corporation. Such a business may also be transacted by a life insurance corporation. Thus, the fact that a corporation transacts an annuity business is not, of itself, significant in determining the character of the corporation.

The District Court, in addition to misapplying the "activities doctrine" as stated in its opinion, further erred in accepting the contention also made here that there is any such doctrine recognized by the authorities in construing the exclusion provision of Section 4. The debtor, the trus-

tee and the Securities and Exchange Commission rely for the most part on cases such as *Cate v. Connell*, 173 F. 445 (CCA 1st, 1909), *In re Kingston Realty Co.*, 160 F. 445 (CCA 2d, 1908), *In re Interstate Paving Co.*, 171 F. 604 (D. C. N. Y., 1909), arising under Section 4 prior to its amendment by Act June 25, 1910, c. 412, 36 Stat. 839. The inapplicability of these cases was pointed out by the Circuit Court of Appeals. They arose under the statute at a time when it provided that the amenability of a corporation to involuntary bankruptcy was to be determined by its principal pursuit. It was to avoid the uncertainty and confusion produced by the application of the statutory activities test that the 1910 amendment was made.

Gamble v. Daniel, 39 F. (2d) 447 (CCA 8th, 1930).

Another line of authority upon which the petitioners and the Securities and Exchange Commission rely is constituted by cases such as *In re Roumanian Workers Educational Ass'n.*, 108 F. (2d) 782 (CCA 6th, 1940), which are concerned with determining whether a corporation is a "moneyed, business or commercial corporation" within the meaning of Section 4. The inapplicability of these cases was likewise pointed out in the opinion by the Circuit Court of Appeals.

The only case which directly supports petitioners' view as to the existence of an "activities doctrine" is *In re Supreme Lodge of the Masons Annuity*, 286 F. 180 (N. D. Ga., 1923), which is contrary in that respect to the decisions of the Court of Appeals for that circuit. *Cf. Grand Lodge, Knights of Pythias v. McKee*, 95 F. (2d) 474 (CCA 5th, 1938). In that case the court remarked that the charter powers of a corporation should be resorted to in most in-

stances for the purpose of determining its classification, and that in extreme cases resort might be had to activities rather than charter powers. The court by way of illustrating the application of the "activities doctrine" referred to a Georgia corporation which had obtained an ancient grant of a charter containing power to operate a railroad and a bank. It remarked that the company at no time had operated a bank, and that in order to determine its character the business actually done under its charter should control.

It may be that in a proper case there would be occasion to resort to an "activities doctrine." If under state law a corporation in a particular case were not clearly classified and if its charter powers and activities were broad enough to include operations both within and without the fields in which insurance, banking, building and loan corporations, etc. usually operate, a court might find it necessary to look to the business actually done, or to those charter powers actually exercised, in determining the true character of the corporation. Such, however, is not the case here, and it is not probable that such a case will often arise. Insurance, banking, building and loan and railroad corporations are almost universally regarded as being affected with a public interest and are closely regulated by the states. In line with this regulation, the purposes for which such corporations may be organized are usually defined to exclude non-related enterprises. This is certainly true in the field of life insurance. A study of the statutes relating to life insurance corporations which we have set out at pp. 63 to 75 of the Appendix indicates the uniformity of the law of the various states, certainty of classification, and the exclusion of non-related enterprises.

F. The petitioners' contention that the Investment Company Act of 1940 has defined the term "insurance corporation" as used in Section 4 of the Bankruptcy Act, as amended in 1910, and that, as so defined, Fidelity is not an insurance corporation, is without merit

The petitioners contend in this court that even if the term "insurance corporation," as inserted in Section 4 of the Bankruptcy Act by the 1910 amendment, was not defined, it has now been defined by the Investment Company Act of 1940 and that, as so defined, the term does not include Fidelity. Under the Investment Company Act of 1940 the term "face amount certificate" is created and defined (15 U. S. C. A., sec. 80a-2 (a) (15)). The term embraces both life and term annuities and other comparable contracts which are not material here. The term "investment company" is also created and defined (15 U. S. C. A., sec. 80a-3 (a) (2)). An "investment company" is a company issuing face amount certificates or other defined types of investment contracts. The term "face amount certificate company" is created and defined (15 U. S. C. A., sec. 80a-4 (1)). A "face amount certificate company" is an investment company dealing in face amount certificates. Since any annuity is a face amount certificate, and since companies dealing in face amount certificates are face amount certificate companies, all life insurance companies would be regulated under the Investment Company Act, were it not for the exclusion made by 15 U. S. C. A., sec. 80a-3 (c) (3) and 80a-2 (a) (17). These sections define and exclude insurance companies from the definition of "investment companies" and "face amount certificate companies." As so defined and excluded, insurance companies are those whose

primary and predominant business activity is the writing of insurance policies and which are subject to supervision by the insurance officials of the various states.

In addition to providing extensive regulation for face amount certificate companies and other investment companies, the Investment Company Act of 1940 amended two sections of the Bankruptcy Act, namely Section 44 (a) (11 U. S. C. A., sec. 72 (a)) dealing with the appointment of trustees in bankrupt estates and Section 67 (11 U. S. C. A., sec. 107) dealing with liens upon, and fraudulent transfers of, the property of bankrupts. The amendment of Section 44 (a) provided that if a bankrupt were a face amount certificate company, the court should appoint the trustee upon giving the Securities and Exchange Commission an opportunity to be heard, and the creation of Section 67 (f) provided a method for equalizing the distribution in bankruptcy of state deposits made after January 1, 1941 by face amount certificate companies.

The petitioners argue that on the basis of these provisions of the Investment Company Act of 1940, the Congress has created a type of company known as a face amount certificate company; that the term "face amount certificate company" is created, among other things, for the purpose of the Bankruptcy Law; that it is clearly contemplated that face amount certificate companies may become bankrupts; that face amount certificate companies include insurance corporations whose primary and predominant business does not consist of writing insurance policies, and that consequently no face amount certificate company is an insurance corporation within the meaning of Section 4 of the Bankruptcy Act, as amended in 1910, excluding such corporations from bankruptcy.

This argument was not advanced in the court below and is not pressed in this court by the Securities and Exchange Commission.[1]

In enacting the Investment Company Act of 1940 Congress specifically directed its attention to amending the Bankruptcy Act. That act was amended in two particulars, neither of which related to the provisions (Section 4) specifying those who might become bankrupt. Both of the amended sections, 44 and 67, relate to the administration of assets of those who have been adjudged bankrupt. Had Congress intended to deal with the question of those who might become bankrupt, it could easily have done so. Had it intended to define the term "face amount certificate company" for purposes of Section 4 of the Bankruptcy Act and to provide that the undefined term "insurance corporation" used in that section should not include a face amount certificate company, it could easily have done so by express language. It is unbelievable that it could have intended to do these things through the process of tenuous indirection contended for.

The fact that Section 4 remained unchanged in the face of the other specific changes in the act is in itself persuasive that Congress addressed itself to the subject of

---

[1]The Securities and Exchange Commission, however, advances the contention that if insurance corporations are to be classified according to the law of the state of incorporation, as held by the court below, the result may be that the definition of the term "insurance company" under the Investment Company Act of 1940 may be affected. We can see no ground for such a contention. Under the Investment Company Act of 1940 the term "insurance company" as there used is defined as a company whose primary and predominant business activity is the writing of insurance. The definition of that term for the purposes of that act would necessarily control in the application of that act. The fact that for the purposes of the Bankruptcy Act the term "insurance corporation" may be judicially defined otherwise in the absence of legislative definition, in no way bears upon the administration of the Investment Company Act. The term "insurance corporation" may have a different meaning as defined for the purposes of different acts. See 26 U. S. C. A., sec. 201 (a), where life insurance companies are defined for purposes of taxation, and 15 U. S. C. A., sec. 605i, where they are defined for purposes of Reconstruction Finance Corporation lending. A face amount certificate company could be a life insurance corporation for purposes of taxation or purposes of RFC lending, even though it were not an insurance company for the purposes of the Investment Company Act of 1940. There is no reason why the same difference could not exist between the Investment Company Act and the Bankruptcy Act.

changing the act and intended no changes other than those expressly provided for.

Sampayo v. Bank of Nova Scotia, 313 U. S. 270, 85 L. ed. 1324, 61 S. Ct. 953 (1941)

No one contends that face amount certificate companies were first made amenable to the Bankruptcy Act by the Investment Company Act of 1940. While the term was first defined in the Investment Company Act, the companies to which it was applied had long been in existence and many of them were subject to the Bankruptcy Act as "moneyed, business or commercial corporations" not otherwise exempt as insurance corporations, etc. under Section 4. During its existence as an annuity company under West Virginia law Fidelity was subject to the Bankruptcy Act. Those who framed the Investment Company Act were obviously aware that such companies were amenable to bankruptcy, and there is no reason to suppose that in amending the Bankruptcy Act they were doing anything other than providing for the administration in bankruptcy of the assets of those companies.

The doctrine of implied amendment and implied repeal is not favored. If a subsequent statute which does not expressly change an existing provision can be given effect without being interpreted as so amending the provision, it will not be regarded as having been intended to do so.

Nelson v. Nelson, 209 P. 810, 72 Colo. 20;

Hamilton County Bd. of Com'rs v. State, 111 N. E. 417, 184 Ind. 418;

People v. Illinois Cent. R. Co., 145 N. E. 719, 314 Ill. 339;

Starbird v. Brown, 24 A. 824, 84 Me. 238, 240;

and see, generally, cases cited in 59 C. J. 857. Applying this rule to the situation at hand, it is evident that no amendment of Section 4 of the Bankruptcy Act can be implied. (There is no contention of an express one.) Had face amount certificate companies been excluded from bankruptcy prior to the enactment of the Investment Company Act which made provision for their administration in bankruptcy, they would impliedly have been made amenable to the Bankruptcy Law. The provision for the administration of their assets would have been inconsistent with their exclusion. However, since there were face amount certificate companies as defined in the Investment Company Act which were amenable to bankruptcy prior to the enactment of the Investment Company Act, there is no ground for supposing that Congress intended going further than to provide for administering the assets of such companies. There is no reason to suppose that Congress intended to provide for the administration of the assets of face amount certificate companies otherwise excluded by the Bankruptcy Act and thus to amend the excluding provisions. The term "insurance corporation" as used in Section 4 of the Bankruptcy Act can be given the meaning attributed to it by the courts without in any way conflicting with the Investment Company Act of 1940. The term "face amount certificate company" and the term "insurance company" as used in the Investment Company Act of 1940 can be given full effect without in any way conflicting with the judicial interpretation of the term "insurance corporation" as used in Section 4 of the Bankruptcy Act. Under such circumstances there is no room for the doctrine of implied amendment.

It is established, in view of the foregoing, that in enact-

ing the Investment Company Act of 1940 Congress did not intend to supersede the judicial definition of the term "insurance corporation" as used in Section 4 of the Bankruptcy Act and that the decisions relied upon by the court below remain authoritative.

G. The question as to whether the debtor is an insurance corporation is to be determined by its status at the time the petition was filed. At that time it was an insurance corporation. It is not material that prior to December 31, 1940 it was not an insurance corporation or that the major portion of its assets and liabilities was acquired prior to the time it became an insurance corporation

We have pointed out that the debtor was incorporated as an insurance company in West Virginia on December 31, 1940 and that it was licensed and did business as such in West Virginia. At the time the present proceedings were instituted, June 6, 1941, the debtor had been placed in receivership by the Insurance Commissioner under the provisions of West Virginia law. It was not at that time transacting any business, except such as was transacted through the receivers. For purposes of this proceeding, however, we look to its status at the inception of the receivership.

In re Peoria Life Ins. Co., 75 F. (2d) 777 (CCA 7th, 1935);

In re Union Guarantee & Mortgage Co., 75 F. (2d) 984 (CCA 2d, 1935).

At that time the debtor existed as an insurance corporation under West Virginia law.

It seems to be the contention of the petitioners and the Securities and Exchange Commission that since the

debtor acquired the status of an insurance corporation but a few months prior to the time it was taken over by the Insurance Commissioner, its status as such a corporation should be disregarded in these proceedings. Thus, the petitioners stress the argument that a corporation should not be permitted to change its classification to that of a corporation excluded from bankruptcy and thereby to deny its creditors the benefits of bankruptcy. The Securities and Exchange Commission emphasizes that the principal assets and liabilities of the debtor were acquired prior to the time it became an insurance corporation; that it is such assets and liabilities which are to be administered, and that accordingly it should be regarded as occupying the status it had during the time it acquired the assets and liabilities. We may note parenthetically that the record does not show a comparison of the assets and liabilities acquired by Fidelity before and after December 31, 1940. After that time it received substantial amounts of money and incurred substantial obligations on its contracts. It also acquired liability under its insurance contracts, although the extent to which claims may arise out of such contracts will be contingent upon factors such as whether the re-insurance agreement is continued.

The contention of the petitioners is clever. It stresses the denial to creditors of the benefits of bankruptcy through change in the debtor's status. One would almost think that the creditors had instituted this proceeding. But such is not the case. It was instituted by the debtor. In the very nature of things different considerations must obtain in the two cases.

Chicago T. & T. Co. v. Forty-One Thirty-Six W. Corp., 302 U. S. 120, 82 L. ed. 147, 58 S. Ct. 125 (1937);

The right of the creditors is amply provided for by permitting them to file an involuntary petition in a proper case.

On December 31, 1940 the debtor applied to West Virginia for permission to incorporate as a life insurance corporation under West Virginia law. The permission was granted. It invoked the protection of West Virginia law,—it assumed the status of a life insurance corporation under West Virginia law for purposes which it considered beneficial to it. The regulatory provisions of the Investment Company Act of 1940 became effective January 1, 1941, one day following the debtor's incorporation as a life insurance company. It has been conceded by everyone in this case that the change was made for the purpose, among others, of escaping the regulatory provisions of the Investment Company Act. As to just how this was to be done has not yet been fully disclosed. Several theories are plausible. But whatever its plan may have been, the debtor thought that by assuming the status of a life insurance corporation under West Virginia law its chances of continuing in business would be enhanced.

West Virginia has enacted regulation appertaining to the incorporation and supervision of life insurance companies.[2] The debtor voluntarily assumed the status of a life insurance corporation in West Virginia. But after some months of effort, it found itself unable to continue business. It then utilized its corporate authority, enjoyed by virtue

---

[1]The Supreme Court did not accept all the reasoning of the Circuit Court of Appeals. Cf. **Marine Harbor Properties, Inc. v. Manufacturer's Trust Co.**, ——, U S ——, 87 L. ed. (adv.) 73, 63 S. Ct. 93. But we do not understand that the lower court was overruled on the proposition to which it is cited.

[2]It was because of the adequacy of such regulation, including liquidation and reorganization proceedings, that insurance corporations were excluded from the Bankruptcy Act (ante, p. 74).

of its existence as a West Virginia life insurance corporation, and filed a petition in federal District Court denying that it was a life insurance corporation and basing its claim for relief upon that denial. These facts speak for themselves.

As to the claim that the debtor's status at the time it acquired the major portion of its assets and liabilities should control, there are helpful precedents.

The Bankruptcy Act has long provided for voluntary petitions by farmers and wage earners, but it has exempted them from involuntary proceedings (Section 4 (b), 11 U. S. C. A., sec. 22 (b)). Since natural persons are by nature empowered to engage in an infinite variety of occupations, it has been necessary to define the terms "wage earner" and "farmer" upon the basis of their primary and principal activities (Section 1 (17), (32), 11 U. S. C. A., sec. (1) (17), (32)). In administering the Bankruptcy Act cases have occurred where one incurred assets and liabilities as a farmer and thereafter engaged in an occupation not exempt from involuntary bankruptcy. Other cases have occurred where persons have incurred assets and liabilities in an unexempt occupation and have thereafter assumed the status of a wage earner or farmer. There is some authority for the proposition that the status of a farmer or wage earner for the purpose of amenability to bankruptcy is to be determined as of the time that his assets and liabilities were acquired.

In re Burgin, 173 F. 726 (D. C. Ala., 1909);

In re Crenshaw, 156 F. 638 (D. C. Ala., 1907).

It is the general rule, however, that status is to be determined as of the time of an act of bankruptcy.

Smith v. Brownsville State Bank, 15 F. (2d) 792 (CCA 8th, 1926);

Flickinger v. First National Bank, 145 F. 162 (CCA 6th, 1906);

Counts v. Columbus Buggy Co., 210 F. 748 (CCA 4th, 1913);

In re Inman, 57 F. (2d) 595 (D. C. Wyo., 1932);

In re Folkstad, 199 F. 363 (D. C. Mont., 1912);

1 Remington on Bankruptcy (4th ed.) 175.

The status of a person during the time when assets and liabilities were acquired is held by the weight of authority to be material only in so far as it bears upon what his chief occupation was at the time an act of bankruptcy was committed.

Powers v. Silberman, 3 F. (2d) 802 (CCA 3rd. 1925);

In re Brown, 253 F. 357 (CCA 9th, 1918);

In re Inman, 57 F. (2d) 595 (D. C. Wyo., 1932);

In re Brown, 284 F. 899 (D. C. Mo., 1922);

In re Disney, 219 F. 294 (D. C. Md., 1915).

In order to remove any doubt about the question Congress, following the majority rule, has enacted that the status of a person as a farmer or wage earner is to be determined as of the time an act of bankruptcy is committed. (Bankruptcy Act, Section 22 (b), as amended by Act June 22, 1938, c. 575, sec. 1, 52 Stat. 845). It is thus the legisla-

tive policy that status at the time assets and liabilities are acquired is not determinative.

In re Harriman, 31 F. Supp. 50 (D. C. N. Y., 1939)

By analogy to the cases and congressional policy dealing with the status of a person as a farmer or wage earner, the status of a corporation at the time of acquiring the major portion of its assets and liabilities should not determine its amenability to bankruptcy.[1] In a case of ordinary bankruptcy, even where the proceedings are involuntary, the status of the corporation at the time of the alleged act of bankruptcy should govern, although it may be conceded that a corporation could not, shortly before such an act, join the class of those excluded from bankruptcy with the intention of avoiding an involuntary petition.

In re Inman, 57 F. (2d) 595 (D. C. Wyo., 1932).

So far as Chapter X is concerned, we may assume that a similar rule would obtain. We may assume that if a corporation committed an act of bankruptcy and thereafter changed its classification within four months, it would nevertheless be amenable to an involuntary petition at the suit of its creditors (Bankruptcy Act, Section 131, 11 U. S. C. A., sec. 531). We may assume, moreover, that if any of the other matters had occurred, which under Section 131 invest creditors with the right to institute involuntary proceedings, a corporation could not thereafter change its status while the basis for jurisdiction continued to exist. Since this suit is not instituted by creditors, however, the question is not material and, even if it were, no basis would be

---

[1] Neither is it significant in determining the status of a corporation at any other time, since the corporate exclusion provision is not based upon a principal, activities test by Section 4 or by the decisions construing it.

afforded for holding the debtor amenable to Chapter X under the facts of the case. We may also assume that a corporation could not change into an excluded class for purposes of avoiding a Chapter X petition by creditors knowing that shortly thereafter it would commit an act of bankruptcy or suffer one of the contingencies to befall it which constitute a ground for the filing of an involuntary petition. But there is no evidence that Fidelity changed its classification with any such idea in mind, and none of those supporting the petition have ever ventured the suggestion that it entertained such an idea.

II

THE PETITION FOR REORGANIZATION WAS NOT FILED IN GOOD FAITH

Assuming for the purpose of argument that debtor were not an insurance corporation, its petition was not filed in good faith.

A. Statutes

Section 130 (7) of Chapter X of the Bankruptcy Act, Act June 22, 1938, 52 Stat. 883 (11 U. S. C. A., sec. 530 (7)), provides that every petition shall state "the specific facts showing the need for relief under this chapter and why adequate relief cannot be obtained under chapter 11 of this act."

Section 144 of Chapter X (11 U. S. C. A., sec. 544) provides:

> "If an answer filed by any creditor, indenture trustee, or stockholder shall controvert any of the material allegations of the petition, the judge shall, as soon as may be, determine, without the intervention of a jury, the issues presented by the pleadings and enter an order approving the petition, if satisfied that it complies with the requirements of this chapter and has been filed in good faith and that the material allegations are sustained by the proofs, or dismissing it if not so satisfied."

Section 146 of Chapter X (11 U. S. C. A., sec. 546), insofar as material here, provides:

> "Without limiting the generality of the meaning of the term 'good faith,' a petition shall be deemed not to be filed in good faith if—
>
> "(1) * * *
>
> "(2) * * *

"(3) it is unreasonable to expect that a plan of reorganization can be effected; or

"(4) a prior proceeding is pending in any court and it appears that the interests of creditors and stockholders would be best subserved in such prior proceeding."

B. The petition should have been dismissed pursuant to Section 146 (3) on the ground that it was unreasonable to expect that a plan of reorganization could be effected

1. The question as to whether the petition was filed in good faith within the meaning of Section 146 (3) of Chapter X was raised in the District Court and in the Circuit Court of Appeals and is open for argument in support of the judgment of the Circuit Court of Appeals.

In *Ryerson v. United States*, 312 U. S. 405, 85 L. ed. 917, 61 S. Ct. 656 (1941), it was held that a respondent in a matter brought before the court by certiorari might advance any proposition in support of the judgment of the court below which was argued in that court.

2. The purpose of Chapter X is to provide for the rehabilitation of corporations as going concerns, and the provisions of Section 146 (3) were framed in the light of that purpose. Neither the debtor's petition nor the proof demonstrates that it is entitled to the benefits of Chapter X.

a. The purpose of Chapter X and the requirements under Section 146 (3)

The fundamental purpose of Chapter X and its predecessor, Section 77B, was to provide means for the rehabilitation of corporations in order to preserve values inherent

in their continuance as going business enterprises. The purposes of Chapter X are sharply distinguished from the purposes of straight bankruptcy or other proceedings, having for their purpose the liquidation of the assets of business concerns and their distribution to creditors. This fundamental difference is explained at pp. 2-3 of Finletter, Law of Bankruptcy Reorganization (1939 ed.), where it is said:

> "Now there is one underlying fact about these laws (and their successors, the reorganization chapters of the 1938 Act) which colors their whole quality. They are not bankruptcy laws at all. Bankruptcy procedure is a method of liquidation, and the reorganization provisions of the Act are codifications of the old federal equity receivership whose purpose is the opposite one of reorganization. *The rules of law which make up the equity procedure were conceived with reference to the continuance of the enterprise as a going concern.* The statutes and decisions which constitute the law of bankruptcy were formed with the object of liquidating the business and obtaining the maximum amount of cash for distribution to the creditors. The interpretation of the new reorganization chapters of the Act accordingly must recognize their real ancestry. The principles of the equity receivership underlie nearly every substantive provision of the new amendments.
>
> "The reason that the new laws are in the Bankruptcy Act is entirely a question of constitutionality. * * *" (Emphasis supplied) Finletter, Law of Bankruptcy Reorganization (1939 ed.) pp. 2-3.

See entire discussion of "Origins of Reorganization Provisions," Finletter (1939 ed.), pp. 1-35, and

Warner Bros. Pictures v. Lawton-Byrne-Bruner Ins. A. Co., 79 F. (2d) 804, 810-811 (CCA 8th, 1935).

As said in *In re Dutch Woodcraft Shops*, 14 F. Supp. 467 (D. C. W. D. Mich., 1935):

> "Obviously, the essential purpose of section 77B is to preserve and continue a going business but in cases where going concern values have been wholly or practically eliminated, the case is one for liquidation rather than for reorganization. The preservation of business enterprises must not be at the expense of creditors, and the provisions of sec. 77B should not be taken advantage of to effect what, in fact, amounts to a composition under sec. 12 (11 U. S. C. A., sec. 30)."

See citation of a portion of the foregoing language and discussion of the *Dutch Woodcraft Shops* case in *Case v. Los Angeles Lumber Products Co.*, 308 U. S. 106, 84 L. ed. 110, 60 S. Ct. 1 (1939) (at 308 U. S., footnote 120-121).

Section 146 of Chapter X, the "good faith" provision, and subsec. (3) thereof must be interpreted, as were the "good faith" provisions of Section 77B, in the light of the fundamental purpose of Chapter X. Good faith was found wanting in Section 77B proceedings where the debtor could not meet the burden of proof upon it to show that it could be reorganized as a going concern, and under such circumstances such petitions were dismissed.

An illustrative case was *First National Bank v. Conway Road Estates Co.*, 94 F. (2d) 736 (CCA 8th, 1938), cert. den. 304 U. S. 578, 82 L. ed. 1541, 58 S. Ct. 1047, where the issue of good faith was passed upon prior to the submission of a plan of reorganization on motion by a lien holder to dissolve a temporary injunction restraining foreclosure. The language of the case is apposite here. It was said:

> "In a reorganization proceeding under section 77B good faith means more than honesty of purpose. It also

requires that there be a reasonable possibility of successful reorganization. Wright v. Vinton Branch Bank, 300 U. S. 440, 463, 57 S. Ct. 556, 562, 81 L. Ed. 736; Tennessee Publishing Co. v. American Bank, supra; In re. Tennessee Publishing Co., 6 Cir., 81 F. 2d 463; In re Loeb Apartments, 7 Cir., 89 F. 2d 431; Manati Sugar Co. v. Mock, 2 Cir., 75 F. 2d 284; O'Connor v. Mills, 8 Cir., 90 F. 2d 665; Provident Ins. Co. v. University Church, 9 Cir., 90 F. 2d 992.

"Whenever want of good faith appears the debtor's petition should be dismissed even though a plan of reorganization has not been submitted. The District Court was reversed for failure to dismiss in such a case in Provident Ins. Co. v. University Church, supra, in Re Wisun & Golub, 2 Cir., 84 F. 2d 1, and in Re North Kenmore Corporation, 7 Cir., 81 F. 2d 656. The judgment of the District Court dismissing the petition for want of good faith was affirmed in O'Connor v. Mills, supra; in Manati Sugar Co. v. Mock; supra; and in Re Gribsby-Grunow Co., 7 Cir., 77 F. 2d 200.

"In Brockett v. Winkle Terra Cotta Co., 8 Cir., 81 F. 2d 949, 953, Judge Valkenburgh, speaking for this court, said in reference to section 77B: 'The outstanding purpose of the Amended Act, upon which this case rests, was to afford aid in the effort to rehabilitate corporations solvent in fact but unable to meet maturing obligations.' It was not the purpose to lend its aid generally and without discrimination to corporations hopelessly insolvent, and without legal resources to prosecute their business with reasonable prospect of success.

"Considering the act itself and all these decisions it is apparent that it is the duty of the District Court to bear in mind the purpose and function of 77B at every step of the proceedings; and whenever it appears that

rehabilitation of the debtor is impracticable or that injunctive relief is not sought in good faith the court in the exercise of a sound discretion should refuse the debtor further aid in harassing lienholders. * * *" (94 F. (2d) 739)

Other cases similarly decided under Section 77B, in addition to those cited in the above case, are:

Price v. Spokane Silver and Lead Co., 97 F. (2d) 237 (CCA 8th, 1938); cert. den. 305 U. S. 626, 83 L. ed. 401, 59 S. Ct. 88;

Sophian v. Congress Realty Co., 98 F. (2d) 499 (CCA 8th, 1938);

Milwaukee Postal Bldg. Corp. v. McCann, 95 F. (2d) 948, 950 (CCA 8th, 1938);

Sartorius v. Bardo, 95 F. (2d) 387 (CCA 2d, 1938);

In re Island Park Associates, 77 F. (2d) 334, 337 (CCA 2d, 1935);

In re Greyling Realty Co., 74 F. (2d) 734, 736 (CCA 2d, 1935);

In re Prudence-Bonds Corp., 77 F. (2d) 328, 330 (CCA 2d, 1935);

In re 235 West 46th Street Co., 74 F. (2d) 700 (CCA 2d, 1935);

and see:

Old Fort Improvement Co. v. Lea, 89 F. (2d) 286, 289 (CCA 4th, 1937);

48 Harvard Law Review 283.

And it seems clear that this court, as well, recognized the basic proposition that the sole purpose for which 77B pro-

ceedings might be maintained was to "rehabilitate" or "resuscitate" corporations as distinguished from the liquidation of their assets. It said in *City Bank Farmers Trust Co. v. Irving Trust Co.*, 299 U. S. 433, 81 L. ed. 324, 57 S. Ct. 292 (1937):

> "The purpose of § 77B was to facilitate rehabilitation of embarrassed corporations by a scaling or rearrangement of their obligations and shareholders' interests, thus avoiding a winding up, a sale of assets, and a distribution of the proceeds. * * *" (299 U. S. 438)

And in *Tennessee Publishing Co. v. American National Bank*, 299 U. S. 18, 81 L. ed. 13, 57 S. Ct. 85 (1936):

> "Nor do we need to inquire as to the precise limits of the concept of 'good faith' as required by sec. 77B. Whatever these limits may be, the statute clearly contemplates the submission of a plan of reorganization which admits of being confirmed as 'fair and equitable' and as 'feasible.' However honest in its efforts the debtor may be, and however sincere its motives, the District Court is not bound to clog its docket with visionary or impracticable schemes for resuscitation." (299 U. S. 22)

As said in *Marine Harbor Properties, Inc. v. Manufacturer's Trust Co.*, —— U. S. ——, 87 L. ed. (adv.) 73; 63 S. Ct. 93 (Nov. 9, 1942):

> "* * * Section 146 [of Chapter X] represents a codification of some of the interpretations which the courts had given the words 'good faith' in proceedings under sec. 77B. S. Rep. No. 1916, 75th Cong., 3rd Sess., p. 27. * * *" (87 L. ed. (adv.) 75)

That such codification of prior interpretations of the good faith provisions of Section 77B was made in the light of the cases cited thereunder to which we have just referred, and similar cases, is clear from the statements made at hearings held before the Committee on the Judiciary of the House of Representatives from June 1 to June 9, 1937, inclusive. Mr. Weinstein, member of the National Bankruptcy Conference, in explaining the definition of "good faith" in Chapter X, said in part (p. 140 of Hearing before the Committee on the Judiciary, House of Representatives, 75th Cong., 1st Sess., on H. R. 6439):

> "Now, as I indicated a while ago in connection with the approval of the petition, we have carefully defined the meaning of the phrase 'good faith' that is not defined in 77B. It may be anything that the judge says it means, and there have been decisions and there have been variances, and in some instances they are conflicting. One court has set up one standard and another court set up another standard. We have correlated these decisions and have taken out of the decisions what we believe to be the proper standards for determining good faith in the filing of the petition. We have also related good faith to what we tried to do in II, in respect to keep[ing] out companies that have no place in II, that ought to go under subsection I. I have read the definition of good faith and will not tire the committee by repeating it."

The date of Senate Report No. 1916, 75th Congress, Third Session, referred to in the *Marine Harbor Properties* case was April 20, 1938 and is obviously similar in substance to the statements of Mr. Weinstein previously made in June, 1937 at the House Judiciary Committee hearing.

Cases decided under Chapter X involving subsec. (3)

of Section 146 consequently hold that petitions for reorganization must be dismissed where the debtor cannot meet the burden of proof upon it to show that the corporation can be reorganized as a going concern.

In re Julius Roehrs Co., 115 F. (2d) 723 (CCA 3rd, 1940);

In re Suburban Properties, Inc., 110 F. (2d) 438 (CCA 7th, 1940);

Chapman Bros. Co. v. Security-First Nat. Bank, 111 F. (2d) 86 (CCA 9th, 1940);

San Francisco Laundry Ass'n v. American Trust Co., 127 F. (2d) 187 (CCA 9th, 1942);

In re Ware Metal Products, Inc., 42 F. Supp. 538 (D. C. Mass., 1941).

We had not thought the proposition open to doubt that unless the debtor could show that it was reasonable to believe that it could be rehabilitated as a going concern, the petition should be dismissed. The debtor's petition was filed with the declared purpose of having its obligations reduced to a point where it would be solvent and could again continue its business. All of its proof adduced at the hearing was directed toward attempting to show that it could again resume business. During the hearings, however, it became evident to all that Fidelity could never again be a going concern. The Circuit Court of Appeals expressly found and the District Court, as may be fairly inferred from its opinion, was also of the opinion that there was no reasonable prospect of the company being reorganized as a going concern. As stated by the Circuit Court of Appeals, there is "only the immediate need of a liquidation

of the company's assets for the benefit of the contract holders" (R. 259).

Under the authorities which we have cited such a situation required dismissal of the petition. After the hearings, however, it began to be suggested, particularly by the SEC and the federal trustee, that the federal proceedings should continue for the purpose of effecting what was termed a "slow and orderly liquidation," although no testimony had been adduced by any party to show the need for or the desirability of any such procedure. The District Court accepted that view and, insofar as its opinion is referable to Section 146 (3), apparently based its decision on the proposition which it expressed as follows:

> "It is not necessary that there be a reasonable prospect for the successful rehabilitation of the Debtor as a going or continuing corporation. It is sufficient if it is shown that the Debtor is in a position to conform to and obtain the benefits of the statute for a slow, beneficial and orderly liquidation. *R. L. Witters Associates, Inc. v. Ebsary Gypsum Co., Inc., et al.*, 93 F. (2d) 746 (C. C. A. 5th 1938); *Re Central Funding Corporation*, 75 F. (2d) 256 (C. C. A. 2d 1935); *In Re: Mortgage Securities Corporation*, 75 F. (2d) 261 (C. C. A. 2d 1935). * * *." (R. 196)

It is our view that this proposition is wholly erroneous as applied to the facts of this case. Such a construction of subsec. (3) of Section 146 of Chapter X results, under the facts here present, in its complete abrogation. It is difficult to see how a petition for reorganization could ever be dismissed by a creditor or other party in interest on the grounds specified in Section 146 (3), if all a debtor is required to show in order to suspend prior proceedings and

to initiate federal reorganization proceedings is that the assets of the corporation could be liquidated in a "slow and orderly" fashion. This could be done with any assets of any corporation, whatever the circumstances, and the protection afforded creditors by Section 146 would be a mere illusion.

We will analyze the cases cited in the District Court's opinion: In *R. L. Witters Associates v. Ebsary Gypsum Company*, 93 F. (2d) 746 (CCA 5th, 1938), which arose under Section 77B, the District Court had said, among other things.

> "By reference to 'good faith' the meaning is not merely sincerity of intention. The expression embraces a reasonable expectation of continued useful existence. There must be reasonable prospect for successful rehabilitation of the debtor * * *
>
> "Undoubtedly section 77B is aimed at the 'continuance of a business as a going concern,' and does not contemplate an inactive corporation, bereft of its chief means of livelihood. * * *
>
> "Where a case presented is one for liquidation or for composition, proceedings under 77B should not be approved and the rights of creditors must be guarded and recognized throughout the proceedings as paramount to those of stockholders. * * *" (93 F. (2d) 747)

(We may note that language substantially similar to the foregoing was expressly approved in *Case v. Los Angeles Lumber Products Co.*, as cited *ante* at page 100.)

The Circuit Court of Appeals said of this:

> "Appellant insists that the District Judge gave too narrow a construction to the statutory words 'good

faith'; that he gave them a meaning not intended by the lawmakers, and neither expressed nor implicit in the words. It insists that this ruling would exclude from the operation of the statute all corporations except those which are to be reorganized as going concerns; that specifically it would exclude corporations seeking an orderly and conserving liquidation as against the disrupting and dismembering processes of common-law actions and seizures.

"We agree with appellant. The statute as to the corporations eligible to file the petition is broad and comprehensive. Under it, 'Any corporation which could become a bankrupt * * * may file an original petition.' *Nowhere in the statute is there any definition of 'good faith.'* What is meant by the term must be drawn from the meaning of the words themselves; as interpreted by the context in which they are used; the purpose back of the statute, the mischiefs it was enacted to prevent, the results it was enacted to accomplish." (Emphasis supplied) (93 F. (2d) 748)

Judging from this language the Circuit Court of Appeals for the Fifth Circuit apparently adopted the theory that under certain circumstances a corporation might petition for reorganization on the ground that it sought an orderly and conserving liquidation of its assets. Under the numerous decisions which we have cited we believe that it is highly doubtful whether such a construction of the act could be maintained as a broad proposition. The lower court's opinion in the *Witters* case is certainly in line with the authorities to which we have referred. The Circuit Court of Appeals' decision was handed down January 5, 1938 and appears, from the language above quoted, to have been predicated upon the fact that Section 77B contained

no definition of good faith. We have seen, however, that Chapter X does contain an explicit definition of good faith and that as early as June, 1937 at the House Judiciary Committee hearing thereon this definition was stated to be the result of the correlation of previous decisions of the courts on the good faith question. Chapter X became effective June 22, 1938 and there can be no question but that in its enactment Congress intended to adopt the decisions rendered prior to the Circuit Court of Appeals' decision in the *Witters* case. The District Court's opinion in the *Witters* case (19 F. Supp. 648) was handed down June 16, 1937 and the cases relied upon therein must obviously have been the same cases which Congress had in mind in adopting the specific definition of good faith found in Chapter X.

Assuming for the purpose of argument that, as possibly decided in the Circuit Court of Appeals' decision in the *Witters* case, a petition for reorganization could be approved solely on the ground that the debtor sought an orderly and conserving liquidation of its assets, it seems too clear for argument that such a theory of reorganization, if valid at all, must be limited to cases where the debtor can make some showing of "going concern value."

Examination of the opinion of the District Court in the *Witters* case, *In re Witters Associates, Inc.*, 19 F. Supp. 648 (D. C. S. D. Fla., 1937), reveals that prior to the petition for reorganization being filed the debtor had sold all of its property to a corporation known as Cement Sales, Inc. under common control with it, which latter corporation proposed to go into the business of importing foreign cement. The property sold consisted of a warehouse and dock which had cost about $49,000, and was subject to mortgages of approximately $28,000, which mortgages had been assumed

by Cement Sales, Inc. The remainder of the purchase price was the sum of $21,500 to be paid by Cement Sales, Inc. in monthly installments of $200.00 each. The only basis upon which the Circuit Court of Appeals decision could be approved would be, as we see it, on the theory that it had reason to believe that the operation of the business of Cement Sales, Inc., the purchasing corporation, would enable it to pay off the mortgages and also pay for the equity of the debtor company, which equity amounted to approximately $21,500.

The situation there was vastly different from that of Fidelity Assurance Association in this case. Here the debtor has no equity whatever remaining in any of its assets, proceedings had already been commenced for the purpose of liquidating those assets prior to the filing of the petition, and going concern values of any kind are entirely absent.

The case of *In re Julius Roehrs Co.*, 115 F. (2d) 723 (CCA 3rd, 1940), is of particular interest in this regard. There the District Court had dismissed a petition filed under Chapter X as not filed in good faith. In deciding on the good faith question the District Court had required that the debtor file a tentative plan of reorganization and there was general testimony of one of the officers of the debtor as to why it was believed reorganization would be possible and advantageous. The Circuit Court of Appeals in remanding the case to the District Court for further proceedings, said:

> "* * * that it was not the duty of the court to ascertain whether or not a particular plan of reorganization could be carried out but only whether it was reasonable to expect that a plan of reorganization could be effected; that there was opportunity and need for reorganization and that the petition was filed with the

honest intention of effecting it and not for the purpose of hindering and delaying creditors. R. L. Witters Associates v. Ebsary Gypsum Co., Inc., 5 Cir., 93 F. 2d 746; Snyder v. Fenner, 3 Cir., 101 F. 2d 736. Nor is the test whether stockholders will profit by reorganization. It may well be that a plan ultimately adopted would exclude stockholders from any participation. Case v. Los Angeles Lumber Products Co., Ltd., 308 U. S. 106, 131, 60 S. Ct. 1, 84 L. Ed. 110; In re Central Funding Corp., 2 Cir., 75 F. 2d 256, 261. *There is always a question as to whether or not there is a good will or going concern value in the business of a debtor which feasibly may be preserved by reorganization for those entitled to it.* But, as we have already indicated, the petition may not be found to be filed in good faith if it is within any of the prohibitions set forth by Section 146, though it must also be borne in mind that the generality of the meaning of the term 'good faith' is not to be limited by the specific provisions of the section. These are the questions that the District Court must pass on." (Emphasis supplied) (115 F. (2d) 724)

The cases cited by the District Court in the present case cannot, we believe, go beyond the scope of this language.

The case of *Re Central Funding Corp.*, 75 F. (2d) 256 (CCA 2d, 1935), has little, if any, application here. The question of good faith was in no way involved, discussed or decided there. No party had challenged the debtor's good faith. The case involved an appeal from an order confirming a plan of reorganization entered in the lower court. Ninety-four per cent of the debtor's security holders had consented to the plan and only an indenture trustee appealed from the order. The only issue was whether the plan adopted was a plan of reorganization within the mean-

ing of Section 77B (b) (11 U. S. C. A., sec. 207 (b)), (which provisions are similar to those of Section 216 of Chapter X). The opinion does not disclose the factual situation in sufficient detail so that we are able to determine what the decision would have been on the issue of good faith, had such issue been raised. From the language of the court we may deduce that there was some proof in the case which would indicate that the continuance of the business for liquidating purposes only (which apparently had been its only previous function) would produce more for the creditors than a more speedy liquidation. The court did point out:

> "* * * The plan here does not recognize an equity which is of no value, and it arranges simply for the carrying on of the same business conducted by the Central Funding Corporation for a long enough period to enable the new corporation to liquidate advantageously the collateral that secured the bonds that were issued by the debtor. * * *" (75 F. (2d), 259)

Assuming such a case to have a bearing upon the construction of the good faith provisions of Chapter X, it is readily seen that the facts in this case are radically different. Here creditors and others have challenged the debtor's good faith, proceedings have been commenced for the liquidation of Fidelity's assets for their benefit in proceedings expressly adapted to such purpose, and there is no proof whatever that there are any going concern values to be preserved for creditors by a plan of "slow liquidation" which might conceivably be worked out.

In re Mortgage Securities Corporation, 75 F. (2d) 261 (CCA 2d, 1935), is a companion case to the *Central Funding* case and the facts are the same. The question of good faith

was not raised in the case nor touched upon in the short opinion.

The other cases relied upon by appellants, such as *In re Porto Rican American Tobacco Co.*, 112 F. (2d) 655 (CCA 2d, 1940), and *Continental Ins. Co. v. Louisiana Oil Refining Corp.*, 89 F. (2d) 333 (CCA 5th, 1937), are not helpful on the issue of good faith as presented in this case. The issue of good faith was not raised nor in any way decided or commented on in either of these cases. We note that in the *Porto Rican American Tobacco Co.* case the plan apparently contemplated that going concern value would be realized upon by a sale of all of the assets of a subsidiary corporation of debtor to a competing corporation which would operate the same and issue its securities to the debtor's creditors. The *Louisiana Oil Refining* case is cited in the *Porto Rican American Tobacco Co.* case, and while the issue of good faith was in no way raised in the *Louisiana Oil Refining* case, we note that the plan under discussion provided for the continued operation of the business of the debtor by another concern with which it would merge. Such cases are of no assistance here, where the business in which the debtor formally engaged is not to be carried on again but all that remains to be done is to liquidate assets consisting entirely of negotiable securities held in trust by various state authorities to secure contract holders therein. Obviously such procedure would not constitute the reorganization of the business of Fidelity Assurance Association as the term "reorganization" must be interpreted as used in subsec. (3) of Section 146.

That there is a distinction between the cases to which we have referred where the issue of good faith was not raised, and the case at hand where the issue was raised, is

demonstrated by *Sophian v. Congress Realty Co.*, 98 F. (2d) 499 (CCA 8th, 1938). No issue of good faith was raised in that case. The court reviewed a plan of reorganization adopted in the District Court, refused to confirm it, remanded the case for further proceedings and, in so doing, said:

> "The petition of this debtor for reorganization should probably have been dismissed on the ground that it was not filed in good faith. Price v. Spokane, Silver & Lead Co., supra, at page 247. The appellants, however, have not asked that that be done. It is possible that in these proceedings some plan can be worked out which will give to the bondholders all that they are entitled to and will secure the elimination of the valueless stock interest." (98 F. (2d) 502)

It seems too clear for argument that Chapter X was not intended as a mode of liquidating insolvent companies. As said in *Securities and Exchange Commission v. United States R. & Imp. Co.*, 310 U. S. 434, 84 L. ed. 1293, 60 S. Ct. 1044 (1940), where liquidation is indicated, a petition for reorganization must be dismissed *"leaving the debtor to the alternative remedy of bankruptcy liquidation"* (310 U. S. 457).

b. Neither the petition nor the proofs thereon show that debtor is entitled to the benefits of Chapter X; in fact, the contrary is shown

The Petition

The obvious purpose of debtor's petition as filed was to rehabilitate it as a going concern. The proofs adduced by the debtor were directed to showing that it could be rehabilitated as a going concern. When such proofs utterly failed, the SEC and the federal trustee introduced the idea of "slow liquidation" as reorganization, as discussed above. It is obvious from the petition that the debtor is proceeding on a wholly erroneous theory of what may be accomplished in a Chapter X proceeding, even though it did recognize at the outset that the purpose of the proceeding was to enable it to be rehabilitated and continue as a going concern. Paragraph VII of the petition (R. 7-8) reads:

> "Debtor further states that it now has outstanding investment and annuity contracts with reserve liabilities totaling approximately $25,000,000, and that in these contracts debtor agrees to pay interest accumulations of from four to five percent per annum; that the decrease in interest rates in recent years has made it impossible for debtor to invest its funds in conformance with the West Virginia law and to earn the interest requirements as set forth in its said outstanding contracts; and that by reason of said interest requirements under its said contracts debtor is now suffering an annual loss of approximately $250,000 per annum, and that this loss will continue and probably increase unless the earnings on sound securities should increase far in excess of the present rate of income.
>
> "That for the reasons above set forth debtor has been unable to meet its obligations as they mature and will be unable to meet its obligations as they mature

unless the rights of its contract holders are modified so that the earnings received on securities and assets owned by debtor will be sufficient in amount to meet the requirements under its outstanding contracts; and if the rights of its outstanding contract holders are modified to this extent, debtor will be able to comply with the Investment Company Act of 1940 and will be enabled to resume the operation of its business.

"Debtor further states that each of its existing and outstanding contracts is secured under the terms of each of its said contracts by a reserve fund, which is on deposit with the Treasurer of the State of West Virginia and with the officials and departments of other states where the securities of debtor were sold; and that the rights of all contract holders must be modified as above set forth in order that debtor may be permitted to obtain adequate relief, and that by reason of these facts debtor cannot obtain adequate relief under chapter 11 of the Bankruptcy Act."

Debtor thus seeks to carve an equity for itself out of the assets which belong wholly to contract holders. This it cannot do.

Marine Harbor Properties, Inc. v. Manufacturers Trust Co., —— U. S. ——, 87 L. ed. (adv.) 73, 63 S. Ct. 93 (Nov. 9, 1942);

Case v. Los Angeles Lumber Products Co., 308 U. S. 106, 84 L. ed. 110, 60 S. Ct. 1 (1939);

Northern Pacific Ry. v. Boyd, 228 U. S. 482, 57 L. ed. 931, 33 S. Ct. 554 (1912);

and see

Chapman Bros. Co. v. Security-First Nat. Bank, 111 F. (2d) 86 (CCA 9th, 1940).

The petition considered with reference to the state deposit laws

In order to have a clear understanding of just what the debtor seeks to accomplish here we must consider the nature and operation of the state laws, particularly those providing for deposits.

Fidelity was strictly regulated in each state in which it operated. In fifteen of these states, including West Virginia, it had to maintain a deposit as a condition precedent to its obtaining a license to do business therein. The West Virginia deposit was made pursuant to sec. 3, Art. 9, Ch. 33, West Virginia Code.

This section provided that in order to be licensed in West Virginia a deposit in trust of one hundred thousand dollars, and additionally, an amount equal to the total cash liabilities of the company had to be made with the state. The deposit was to be made in securities subject to approval of the insurance commissioner. The deposit requirement was reduced to the extent that the company had securities on deposit elsewhere to secure its liabilities in accordance with the standards of the West Virginia law.

In Wisconsin by sec. 216.02, Wis. Stats. (dealing with "investment associations," App. 1) all of the provisions of Ch. 215 (which relates to the regulation of building and loan associations, App. 2-18) with respect to the supervision, control and conditions upon which foreign building and loan associations are permitted to do business there are made applicable to busiresses such as Fidelity's. By secs. 215.38, 215.39 and 215.395 (App. 3-4) it is provided that a deposit of specified securities shall be maintained as a condition precedent to being licensed to do business there "*in trust* for the benefit and security of all its members in this state", in such amount that the liabilities on

outstanding contracts shall not exceed 90% of the deposit. The deposit is to be held in trust until "all contracts and obligations to persons and members residing in this state shall have been fully performed and discharged." These building and loan association laws were applicable to Fidelity's business and to the deposit made in Wisconsin during all the time it operated there, and thereafter with respect to the liquidation of its Wisconsin assets. Sec. 215.33, Wis. Stats. (App. 8-18).

The laws of the states which require deposits are summarized in the opinion of the Circuit Court of Appeals (R. 241).

Most of these state laws contain detailed provisions for the liquidation of the deposit in the event of insolvency and all provide for the retention of the deposit by the state authority until all claims of residents have been paid in full. The amount of the deposits actually held by the various state authorities, and the liabilities appertaining thereto, is shown, according to debtor's figures, in Ex. 48 (R. 1116 (original)) and a schedule taken therefrom is set forth in the joint statement of facts (*ante*, p. 19).

Fidelity's contracts themselves uniformly contained a provision in Section 1 thereof that the company should maintain certain "reserves" and provided further that "the reserve fund less any unpaid portion of any loans made therefrom on such contracts and any uncollected interest shall be invested in approved securities and deposited in trust as required by the laws of the state of West Virginia" (Exs. 1, 2, 3, 4, 5; R. 170 (original)).

Thus it is seen that all of the contract holders are beneficiaries of state trust deposits, some under the West Virginia trust deposit alone, some under both the West Vir-

ginia trust deposit and the trust deposit in another state and some, such as those in Wisconsin and Iowa, under trust deposits in their own state.

The debtor has made no contention that these trusts are not valid as created and indeed could make no such contention. Such provisions are commonly found in state statutes providing for the regulation of *quasi*-public corporations such as Fidelity and are everywhere sustained as valid enactments. Such laws are discussed generally at 23 Am. Jur. 271 and at 23 Am. Jur. 467, where it is said:

> "* * * the corporation, as well as its stockholders and receiver, is estopped from disputing the validity of a trust upon which the corporation has deposited securities as a condition of the license to do business in the state. * * *"

And see: *United States v. Knott*, 298 U. S. 544, 80 L. ed. 1321, 56 S. Ct. 902 (1936);

Blake v. McClung, 172 U. S. 239, 43 L. ed. 432, 19 S. Ct. 165 (1898) (particularly at 172 U. S. 257);

American United Life Ins. Co. v. Fischer, 130 F. (2d) 643 (CCA 8th, 1942).

The validity of the Wisconsin deposit law (in an earlier form) with respect to deposits required of foreign building and loan associations (Fidelity was regulated as such under Wisconsin law during the time it operated there) has been fully sustained in Wisconsin. *Lewis v. American Savings & Loan Assoc.*, 98 Wis. 203, 73 N. W. 793 (1898).

According to Ex. 48 filed by the debtor (R. 1116 (original)), the market value of all securities on deposit under these laws with the State of West Virginia and with other

states was $20,056,680.27 on June 6, 1941, while the total "net cash liability" to contract holders for whose benefit these deposits were made was, according to that exhibit, $23,475,668.67 as of April 10, 1941. On these figures then, the various state trust deposits are, on a "net cash liability" basis, insufficient to meet Fidelity's present contract liability by a sum in excess of $3,400,000. If Fidelity were again to be licensed so as to continue to do business in the State of West Virginia or in any of these other states requiring deposits, it is clear not only that the present deposits could not be disturbed, but that additions thereto would have to be made in an amount in excess of $3,400,000. To remedy this situation Fidelity, according to the allegations of its petition for reorganization, proposes to reduce its liabilities on its contracts.

Apparently debtor would maintain that while it was necessary to meet the requirements of the state deposit laws in order for it to be licensed to do business in the states, yet as soon as its liabilities exceed those permitted by these laws, it can then, in order to prevent the state authorities from foreclosing on these funds for the benefit of the contract holders, obtain the aid of the federal court in reducing its liabilities to a point where the deposits would again be made whole. Aside from running afoul of the principles of the *Marine Harbor Properties*, the *Los Angeles Lumber Products* and other cases cited above, the sustaining of a petition for reorganization on such a showing would render the state deposit laws of no practical effect or value whatever. Presumably such corporations as the debtor might avoid the effect of the state laws upon which their licenses to do business depended by filing periodic petitions for reorganization in federal court whenever the

deposits might shrink to a value below the requirements of the state laws.

The Proof

Assuming that, despite the obvious deficiency of the petition within the principles and under the facts above discussed, the debtor could be permitted to establish its good faith at the hearing on the controversial answers, if has wholly failed to do so. The burden of proof is of course upon the debtor to establish its good faith in the proceedings, particularly when expressly challenged thereon.

Marine Harbor Properties, Inc. v. Manufacturer's Trust Co., —— U. S. ——, 87 L. ed. (adv.) 73, 63 S. Ct. 93 (1942);

In re Cook, 104 F. (2d) 981 (CCA 7th, 1939);

Hickey v. Ritz Carlton, 96 F. (2d) 748 (CCA 3rd, 1938);

Manati Sugar Co. v. Mock, 75 F. (2d) 284 (CCA 2d, 1935);

In re Scheney Brothers, 12 F. Supp. 609 (D. C. Conn., 1935).

The debtor utterly failed to sustain the burden of proof which is upon it to show, in accordance with Section 146-(3), that it is reasonable to expect that it can be reorganized. It will be recalled that debtor is completely insolvent to the extent of at least three or four million dollars, that it has no license to do business in any state, that it completely suspended the sale of annuity contracts prior to December 31, 1940, that all of its offices have long since been closed, its sales force completely dissipated and lost, and that it is without good will of any sort.

No witness produced by the debtor was able to give the slightest hint as to the manner in which a reorganization could be effected.

John Marshall, Sr., former chairman of the Board, voting trustee, and one of the individuals dominant in the filing of the petition, stated that "I have not any idea of the plan, have not worked on the plan, and don't feel that I am competent to work on it. I have hoped some plan could be worked out" (R. 420), and that "I would not even sit here as a witness and say a plan could be promulgated" (R. 420); "How it is going to be done, I cannot say; I simply don't know" (R. 429).

Mr. McNulty, the debtor's vice president, stated that "There should be additional and new money" (R. 336). He had "not gone into the point of developing any plan" (R. 343). He stated he was a stockholder, had been with the company since 1922, felt attached and devoted to it and "just hopes there is some way to reorganize" (R. 343).

According to Auditor Sims, "The structure of the company economically and financially was unsound from the beginning" (R. 454).

Allen G. Messick, the most recent chairman of the Board, stated that he had been working on the proposition for a year and a half (R. 561). He thought that "a company can be founded on compulsory savings and yield a safe return" (R. 557). He had considered a plan to segregate everything into funds, telling the contract holders what they had, and then "frankly putting it up to them and having them write it down on a relisted basis" (R. 559). He conceded that where contract holders in some states were secured to the full extent of their contracts by deposits, even such a voluntary plan as he proposed would necessarily fail (R. 559).

D. A. Burt, one of the directors, stated that "the first thing of course is to get a plan of such character that new capital can be obtained" (R. 708), but that he did not know whether the company should be continued as a face amount certificate company or in some other form or a combination of more than one form of business (R. 709). He refused to discuss any possible plan, stating, "You are trying to get me to discuss the plan which I will not discuss" (R. 721). In stating that he thought the company could be reorganized he had not considered the authorities of the twenty-nine states in which the company had been licensed (R. 724). He didn't know the basis on which the contracts had been sold in the various states because "we had a regularly organized company to look after those sales" (R. 726).

Carroll D. Evans, formerly a member of the Board and director of sales since 1935, stated that, having in mind the best interests of the contract holders, he could not answer the question as to whether the company should be liquidated or reorganized (R. 933).

The most conclusive testimony to the effect that it is utterly hopeless to expect that Fidelity could succeed either in the sale of annuity or insurance contracts in the future is that of Henry M. Steussy who, during the time Fidelity operated in Wisconsin, was in charge of its operations there.

Mr. Steussy testified that after he left Fidelity he became vice president of Franklin Life Insurance Company. That company, a large and well established concern, had instituted a program whereby a face amount certificate "reconstructed just as the Fidelity contract would have to be reconstructed if the Fidelity Assurance Association was going to operate as an insurance corporation" (R. 1024) was to be sold by that company. It had been qualified for sale

by Franklin in eighteen states (R. 1016). When he had been in charge of Fidelity's Wisconsin operations that office ranked in the top position of all of Fidelity's offices with respect to its sales record (R. 1011). When placed in charge of this program for Franklin he took with him only his best Fidelity salesmen, those who had been able to sell even after the SEC investigation (R. 1026). Franklin had given special training to a group who specialized in selling the annuity type policy for it (R. 1025). The program proved to be a complete failure, however, and these salesmen were unable to sell a sufficient volume of the new Franklin contracts to stay in the business (R. 1026).

Based upon his experience both in Fidelity and in the Franklin Life Insurance Company, he stated that the company could not be reorganized on the seven per cent loading charge permitted by the Investment Company Act of 1940 and could not possibly load the contracts so that it could assemble a sales force and be successful in selling (R. 1039-1040). He stated that Fidelity could not be qualified with the insurance departments in most states of the union (R. 1040).

The competition in the field of savings created by the sale of defense bonds was also shown to make the prospect of future success remote (R. 1043-1046). In view of the fact that government defense bonds may be purchased on monthly payments with the purchaser receiving monthly notices and that the yield is 2.9% (higher than the yield on most of the Fidelity contracts sold since 1934) it is not difficult to see why Fidelity could not hope to meet this competition and the testimony is clear that it could not.

Counsel for the SEC expressly conceded in the Circuit Court of Appeals that the possibilities were "practically

100%" against Fidelity being reorganized as a going concern, and do not argue here that it may be so reorganized. However, the petitioners (the debtor and the trustee) still appear at this late date to be attempting to show that Fidelity can be reorganized as a going concern. In their brief (pp. 44-46) they refer to the testimony of certain witnesses who made statements to the effect that they thought Fidelity could be reorganized. These witnesses specifically refused to venture the slightest suggestion as to how a reorganization might be accomplished or made suggestions so vague as to be entirely without practical meaning. Some of them, as we have shown, testified positively that debtor could not be reorganized. And see testimony of D. A. Burt, R. 715, 718-721, 724, 726, 727; Hubert F. Young, R. 631; Edgar B. Sims, R. 457; H. Isaiah Smith, R. 480, 481, 482, 483; Allen Messick, R. 559-560; Raymond Latta, R. 1111, *et seq.*

"Pell, Ltd." referred to at p. 45 of petitioners' brief, was merely an association of financial men in New York who evinced some interest in purchasing the stock of Fidel Association of New York, a subsidiary of Fidelity, and expressly stated they would make no promises with respect to reorganizing Fidelity (R. 1226). The vague suggestions made in petitioners' brief that Fidelity might be merged with some other investment or insurance company fall far short of meeting the burden of proof on the debtor to show that it can be reorganized.

The District Court made no finding whatever as to whether or not it was unreasonable to expect that a plan of reorganization could be effected. In its opinion it said:

> "* * * It is true that the broad picture developed by the testimony at the hearing does not present a very

favorable view with respect to the rehabilitation and continued operation of the Debtor as a face amount certificate company. * * *" (R. 194-195)

The proponents of the petition were all agreed that any hope of continuance as a going concern would be as a life insurance company (see respondents' joint statement of facts, p. 48-51 *ante*). Assuming for the purpose of argument that debtor was not a life insurance company on the day the petition was filed, it seems obvious that it could not reorganize itself as such under Chapter X.

The District Court further said (R. 195):

> "* * * It is extremely doubtful whether, in view of unsettled economic conditions and the critical international situation, the Fidelity plan would any longer appeal to a large public; *but it is not impossible;* and it is not the duty of the court to decide for the public that investors will not or should not buy these contracts in the future." (Emphasis supplied)

Under the District Court's own interpretation of the testimony, dismissal is unquestionably required under the authorities which we have discussed above. The District Court's opinion (R. 195-196) contains certain statements bearing upon its conclusion that it was "not impossible" for the debtor to resume business. It was said that "the fact that the company has not been operated profitably in the past is not shown to be the result of financial unsoundness in the plan itself." But such statement is completely disproved by the record, particularly the SEC report comprising Ex. 6.

The District Court further stated that it was unsoundness in management methods and extravagant sales and

promotion expenses, useless expenditures for lavish offices including the home office building in Wheeling, West Virginia, and over-expansion particularly in states like Wisconsin where the strictness of regulatory laws made it impossible to operate at a profit, that brought about the company's failure to operate profitably. We do not dispute that these things contributed to its downfall, but nevertheless it was conclusively shown that it was only by these so-called "high-pressure" sales methods that the company could sell its contracts in sufficient volume to continue in business (R. 924).

The District Court stated that the requirements of the Investment Company Act of 1940 were calculated to make the contracts more salable and that this regulatory law has not had the effect of banishing such companies from commercial operation. However, each and every officer of the debtor who testified, and also its general attorney, stated unequivocally that the company could not operate under the Investment Company Act of 1940. And the chief reason for the re-chartering of the company as an insurance company on December 31, 1940 was that the company recognized it was impossible to operate under that Act. The District Court also stated that the testimony discloses that at least one other such company is still in operation "presumably with some measure of success." We take it that by this statement the court referred to the "Investors' Syndicate," a company which operated on the same basis as Fidelity and which was mentioned several times in the testimony. But diligent search of the record on our part does not reveal the economic situation of Investors' Syndicate. The testimony shows that that company some time ago was negotiating with a certain "Chicago Corporation" with

a view to refinancing, and that these negotiations apparently did not succeed (R. 1141). Mr. Pulfer, Fidelity's sales manager in Illinois, testified that he "understood" Investors' Syndicate was still engaged in business and "understood they had a very nice business last year." This is of course the purest hearsay and could form no basis whatever for a conclusion that Investors' Syndicate was operating profitably either in the past or at present. Hubert F. Young, who had charge of Fidelity's investment portfolio, testified that he "understood" that Investors' Syndicate had recently incorporated a new company under the Investment Company Act of 1940, but he stated that he had "no idea" whether that company was now doing business in West Virginia, Wisconsin, Illinois, Tennessee and other states (R. 677). H. Isaiah Smith, one of the West Virginia state court receivers, presently employed by the federal trustee, stated that he did not know whether the Investors' Syndicate was selling face amount certificates today (R. 511). The District Court then remarked that it did not see where the situation of Investors' Syndicate was material because "we may form a new company of Fidelity before we are through with it" (R. 511). We find no other reference to that company anywhere in the record. Neither the SEC, who presumably would have full information as to the operation of Investors' Syndicate under the Investment Company Act of 1940 and previously, nor the debtor, made any attempt whatever to demonstrate that that company, either in its past character or as a new company, had operated or was operating with any degree of success. We refer to the SEC report, Ex. 6, for a discussion of the affairs of Investors' Syndicate.

With respect to all of the unfavorable publicity which Fidelity has received, the District Court stated that all this

had been directed to the unreorganized company and that "it does not follow that if and when the company may be reorganized under the supervision of a United States court, it would retain any of the stigmata which it is the purpose of such reorganization to remove." In view of the undisputed facts as to the effect of this publicity, we can hardly agree with this.

The District Court disposed of the argument that the several states where the debtor had sold its contracts might be unfriendly to future operations of the reorganized company therein by stating "it is sufficient to say that this argument imputes to the governments of those states unworthy motives for future action—motives which no court should assume would be entertained." The District Court wholly failed to consider the nature and effect of the various state laws upon Fidelity's operations, apparently being of the opinion that no discretion whatever resided in state officials as to whether or not the "Fidelity plan" would again be acceptable to those states. The difficulties to be faced may be illustrated by examination of cases in which former efforts of state authorities to ban Fidelity and similar companies are shown.

In *Investors' Syndicate v. Bryan*, 113 Neb. 816, 205 N. W. 294 (1925), affirmed in memorandum opinion by this court, at 274 U. S. 718, 71 L. ed. 1322, 47 S. Ct. 590, the action of the administrative authorities of the state of Nebraska was sustained in denying that company a license to operate there on the basis that the contracts were unfair, unjust and inequitable.

In *Investors' Syndicate v. Porter*, 52 F. (2d) 189 (D. C. Mont., 1931), that company sought to enjoin enforcement of an order of the Auditor and Ex-officio Investment Com-

missioner of Montana, which had revoked the company's license to sell unless the lapsation and other penalties were modified. A three judge district court granted the injunction on the ground that the Montana statute did not give due process. This holding was reversed in *Porter v. Investors' Syndicate*, 286 U. S. 461, 76 L. ed. 1226, 52 S. Ct. 617. In view of the reversal of the district court's judgment, the dissent of one of the district judges is interesting. It provides a complete answer to the contention that the states do not have power under existing law to bar contracts containing such "forfeiture" and "loading" as those involved here on the ground that they are inequitable and unfair to investors.

In *Fidelity Investment Ass'n v. Emerson*, 318 Ill. 548, 149 N. E. 530 (1925), the Secretary of State of Illinois had cancelled Fidelity's license to do business there because the contracts "would work or tend to work fraud upon the purchasers" within the meaning of the Illinois Security Law. Two lower appellate courts sustained the order and it was set aside in the Illinois Supreme Court which found in substance that since the forfeitures were set forth in the contract the contracts could not be said to be fraudulent on their face. The court left open the question as to whether the order might have been sustained if it had been based upon the selling methods used.

We may say that the securities law of Wisconsin, Chapter 189, under which Fidelity's contracts would have to be registered if they were again to be sold there, gives the Securities Department there broad discretion to deny registration if the plan of operation "tends to be unfair, inequitable or fraudulent, or against public interest or the interest of investors." (Sec. 189.13, Wis. Stats. 1941; App.

18-20). The Iowa Securities Act contains similar provisions. (Ch. 393.1, App. 41-50; and Ch. 392 Code of Iowa, App. 37-40). The regulatory laws of other states contain like provisions, and while no state authority could state by way of pre-judgment that Fidelity would not again be admitted there, a realistic appraisal of the situation leads inevitably to the conclusion that, now that the manner in which the "Fidelity plan" operated has been fully disclosed, including the fact that 95% of the investors therein did not carry the contracts to maturity and sustained a net loss upon their investment, such state laws and regulatory authorities would not permit the operation of this type of "plan" again.

C. Prior proceedings are pending which will best subserve the interests of contract holders

The Circuit Court of Appeals held that the petition was not filed in good faith within the meaning of Section 146 (4) of Chapter X, which provides that a petition shall not be deemed to be filed in good faith if a prior proceeding is pending in any court and it appears that the interests of creditors and stockholders would be best subserved in such prior proceeding. This decision was, of course, arrived at in the light of the complete record on file with the court.

In *Marine Harbor Properties, Inc. v. Manufacturer's Trust Co.*, —— U. S. ——, 87 L. ed. (adv.) 73, 63 S. Ct. 93 (Nov. 9, 1942), it is said, in discussing the history and proper interpretation of Section 146 (4) of Chapter X:

> "In view of that history it seems clear that when a prior proceeding is pending, a petitioner's showing of 'need for relief' under Ch. X, required to be con-

tained in every petition by the express provisions of § 130 (7), must demonstrate that at least in some substantial particular the prior proceedings withhold or deny creditors or stockholders profits, advantages, or protection which Ch. X affords. In absence of such a showing the 'need for relief' has not been established and the District Court is not enabled to make an informed judgment on the 'good faith' issue." (87 L. ed. (adv.) 76)

The debtor did not make nor attempt to make, either in its petition or proof, any showing that the prior proceedings pending in the state courts would deny creditors benefits, advantages or protection which Chapter X affords. The petition merely stated that the debtor could not resume business unless its contracts were modified. It thus shows on its face that there is no equity remaining for the stockholders in the assets of the company. The petition recites that certain state court proceedings are pending, but it makes no suggestion that such proceedings are not adequate for the protection of creditors. In fact, it does not even suggest that the proceedings are brought for their benefit.

In arriving at a conclusion under Section 146 (4) of Chapter X the only question involved is whether or not the prior proceedings best subserve the interests of the creditors in this case, the contract holders. Aside from the fact that the debtor wholly failed to make any showing that the prior proceedings would not best subserve the interests of contract holders, the facts as analyzed by the Circuit Court of Appeals show conclusively that the prior proceedings will in fact best subserve the interests of contract holders.

The Wisconsin proceedings

We have previously in this brief set forth the nature of the laws providing for the licensing and supervision of Fidelity and the liquidation of its assets in Wisconsin (*ante*, p. 51-55). The proceedings there were instituted under a complete and detailed scheme providing for the realization of the claims of Wisconsin contract holders out of the assets deposited in Wisconsin. Prior to the filing of the federal petition the Wisconsin contract holders had filed their claims, including the contracts themselves, in the Wisconsin proceedings (Ex. 114, R. 3546 (original), App. 27-36). The Wisconsin contract holders have always looked to and still look to the Banking Commission of Wisconsin to secure to them their proper share of the funds on deposit there. There are some 6000 "active" contract holders in Wisconsin with a total "net cash liability" of approximately $2,340,000. The average "net cash liability" to each of these contract holders is thus between three and four hundred dollars. They purchased the contracts on express representations made to them by debtor as to the security provided by the Wisconsin deposit law. The settlement of any questions arising as to the relative rights of such contract holders in the Wisconsin deposit is amply provided for. It seems almost idle to suggest that the interests of Wisconsin contract holders would be better subserved if each of them is thrown on his own resources and required to employ counsel to prosecute a claim against the Wisconsin deposit in the far-off District Court for the Southern District of West Virginia.

The attitude of the Wisconsin contract holders has been clearly expressed. With singular unanimity they are desirous of severing for once and all their relationship with

Fidelity Assurance Association. Their desire is to have the funds deposited in Wisconsin applied to the just settlement of their claims in an expeditious manner. They are wholly uninterested in reorganization or liquidation plans which may be formulated in the District Court for the Southern District of West Virginia. Their sentiments are expressed in the affidavits of Howard L. Smith and Emmett G. Hampton admitted in evidence here under stipulation as to matters of fact which they contain (R. 3546 (original)), which affidavits comprise Ex. 114 printed at pp. 27 to 36 of the Appendix hereto.

The proceedings pending in Wisconsin are conducted entirely by public authorities under the supervision of a state court, and no liquidator's fees for this service are to be exacted out of the securities deposited there. Counsel for the Banking Commission of Wisconsin in these proceedings have been and are being provided by the Attorney General of Wisconsin at no cost to the contract holders. Prior to the commencement of the federal proceedings and on May 27, 1941, securities comprising a part of the Wisconsin deposit were liquidated and sold, whereby the sum of $1,259,244.04 was realized (Ex. 120, R. 3803 (original)). The prices obtained were substantially in excess of the par value of the securities sold and we have not heard the slightest suggestion that this sale was not conducted in a manner which produced the highest possible prices for these securities. A schedule of the securities so sold and the prices obtained therefor, which is a part of Ex. 120 of the record herein, is printed at p. 26 of the Appendix hereto.

The securities remaining on deposit in Wisconsin are of the highest grade and it is apparent at a glance that they may be liquidated without the slightest difficulty or expense. These securities are:

	Par Value	Market According to Published Quotations 4-14-41
City of Milwaukee— Park 5% 1949	$ 50,000.00	$ 62,812.50
City of Milwaukee— Sewer 5% 1947	30,000.00	37,125.00
City of Milwaukee— Sewer 5% 1948	50,000.00	62,562.50
City of Milwaukee— Sewer 5% 1949	50,000.00	63,062.50
City of Milwaukee— Sewer 5% 1950	25,000.00	32,406.25
United States Treasury— 2⅞—1960-55	160,000.00	175,350.00
United States Treasury— 3¼—1946-44	34,000.00	36,751.88
United States Treasury— ¾ Sept. 1944	800,000.00	798,000.00
	$1,199,000.00	$1,268,070.63

In the face of this situation the filing of the debtor's Chapter X petition has resulted in the Wisconsin proceedings having been held in abeyance since June 6, 1941. We have heard no suggestion that some form of "slow liquidation" plan would result in more money being obtained for these securities than may be presently obtained. To delay their liquidation would only appear to evidence a willingness on the part of the proponents of the petition to speculate with the contract holders' money.

The Iowa proceedings

The proceedings in Iowa were likewise commenced prior to the federal proceedings, and the laws of Iowa pro-

viding for the licensing and supervision of Fidelity and the liquidation of its assets and the proceedings therein, have been described earlier in this brief (*ante*, p. 56-57). The Iowa deposit has been converted to cash.

The proceedings in West Virginia and other states

Neither in the record nor in the District Court's opinion is any suggestion found that the proceedings commenced in the states having deposits other than West Virginia are in any way inadequate or will not secure to the contract holders in those states an economical and speedy method for realizing on the securities deposited for their benefit. Only about one-half of the deposits in dollar amount are located in West Virginia (*ante*, p. 19). With respect to states other than West Virginia, even where the contract holders are not fully secured therein, the situation would seem to be the same as that in Wisconsin and Iowa, as discussed above.

The District Court, while apparently not questioning the adequacy of the proceedings in states other than West Virginia, set forth in its opinion certain considerations upon which it concluded that the West Virginia proceedings would not best subserve the interests of contract holders. We can add little to the discussion of this portion of the District Court's opinion by the Circuit Court of Appeals. In that part of its opinion which relates that one of the West Virginia state court receivers was connected with a law firm whose senior member had been a director of the debtor, the District Court said:

> "* * * It is not improbable that investigation into Debtor's affairs may disclose the existence of liability from some or all of the directors *to Debtor's creditors*. Is it reasonable to suppose that such liabilities, if any,

> would be diligently sought out and pursued in a proceeding with which one of Debtor's directors is so closely associated? * * *" (Emphasis supplied) (R. 198)

As pointed out by the Circuit Court of Appeals no specific facts are set out as to any liability on the part of Fidelity's former directors to its creditors, nor can we find the slightest indication of such in the record. Should such a liability be discovered at some future time, it is difficult to see how a federal trustee could enforce such a liability. We know of nothing in Chapter X which gives a trustee appointed thereunder either the right or duty to enforce claims or causes of action which creditors of the corporation may have against its directors. Section 167 (3) of Chapter X (11 U. S. C. A., sec. 567 (3)) provides that the trustee shall

> "* * * report to the judge any facts ascertained by him pertaining to fraud, misconduct, mismanagement and irregularities, and to any causes of action *available to the estate.*" (Emphasis supplied)

A trustee does not succeed to claims which might exist in favor of individuals against a debtor's directors.

> 1 Gerdes, Corporate Reorganization, para. 405;
>
> Finletter, Law of Bankruptcy Reorganization, pp. 198-199.

Assuming that a federal trustee might prosecute causes of action existing *in favor of the debtor* against individuals, no suggestion was made by the District Court that such a liability exists, nor do we know of anything in the record which would so disclose. The SEC brief stresses "the necessity for impartial investigation" to ascertain whether any such liability exists.

Fidelity has been under investigation by the SEC since prior to 1938. Counsel for the SEC participated in the entire proceedings here but no evidence was adduced and no specific facts are pointed to from which a real possibility that such liability exists could be shown. It seems inconceivable that there could be any fact relative to possible liabilities on the part of individuals to the company which has thus far escaped attention. The SEC brief refers to certain affidavits and pleadings filed by some of its counsel in the injunction suit brought against Fidelity in Detroit in 1938. The allegations of these affidavits and pleadings were expressly denied by Fidelity in its answer to the complaint and the denial was incorporated into the consent decree entered which expressly provided that it was consented to "without admitting the allegations of the complaint and denying past derelictions." See SEC report, Ex. 6, pp. 249-258. Such references made after the full and complete hearing had in this matter will hardly warrant the conclusion that the West Virginia courts and authorities will not perform their duty or that the enforcement of contract holders' rights should be further delayed and jeopardized pending a search for some solvent individual who might be liable to the company on some theory by reason of some past transaction.

It may also be pointed out that one of the West Virginia state court receivers, H. Isaiah Smith, has been placed in charge of Fidelity's affairs to act for the federal trustee, and we cannot conceive how doubts could be expressed as to the adequacy of the West Virginia proceedings in the respect just discussed under such a circumstance.

If interest on the part of state court receivers, as distinguished from the federal trustee, is to be regarded as

controlling in some measure, we believe it is proper to examine the position taken by the federal trustee in this proceeding to date. The federal trustee and its counsel took an active and, we may say leading, part in the trial of the issues presented by the controversial answers to debtor's petition. The federal trustee joins with debtor as one of the petitioners here and throughout has actively opposed at every step the position of those creditors represented in person and by state authorities who oppose the continuance of the federal proceedings. We had thought the provisions of Chapter X, particularly Section 158 thereof (11 U. S. C. A., sec. 558) relating to the disinterestedness of trustees, would necessarily preclude such participation by the trustee.

Under Section 77B it was held that a trustee appointed thereunder was not concerned with the merits of the petition or its dismissal.

> *Loomis v. Gila County*, 101 F. (2d) 827 (CCA 9th, 1939) petition for rehearing denied (with opinion) 103 F. (2d) 312; cert. den. 307 U. S. 643, 83 L. ed. 1524, 59 S. Ct. 1041.

As said in 1 Gerdes, Corporate Reorganization, para. 390:

> "In his relation with creditors and stockholders, the trustee is a fiduciary. His attitude toward all the creditors and stockholders should be the same, and no particular group should be favored over others of the same class."

The participation of the federal trustee in the trial of the issues between the debtor and the respondents here was directly challenged early and late in the hearing

(R. 300, 302, 1166, 1171). After Mr. Fleming, who as we have seen (*ante*, p. 38-40) was instrumental in filing debtor's petition and acted for it in so doing, withdrew from the trial of the issues presented by respondents' controversial answers, he was supplanted by Mr. Ray who also appeared for the debtor in the Circuit Court of Appeals and who appears here. As was pointed out to the Circuit Court of Appeals, the law firm of Mr. Ray is listed as "general counsel" for Central Trust Company, the federal trustee, although this was not known to us at the time of the hearing in the District Court. Mr. Holt, who appeared as counsel for debtor upon the application for the writ of certiorari and who now appears for it, disclosed at the bar of the Circuit Court of Appeals for the Fourth Circuit in connection with debtor's application for stay of mandate, that his law firm was also regularly employed as counsel by Central Trust Company and had in fact been consulted by it in its private interest during the course of the present proceedings in matters affecting those proceedings. We impute no motives to these counsel inconsistent with the highest standards of conduct under Chapter X or under any other standards, but we believe the circumstances indicate a position on the part of the trustee not consistent with the provisions of Section 158 of Chapter X. The independent trustee was referred to by Mr. Justice Douglas, then a member of the Securities and Exchange Commission, at the House hearings on Chapter X, as "the keystone" of the program (p. 165, Hearing before the Committee on the Judiciary, House of Representatives, 75th Congress, First Session on H. R. 6439).

Although, as we have shown, the debtor by its petition and the proof thereon wholly failed to sustain the

burden upon it to show good faith within the meaning of Section 146, the federal trustee has throughout taken upon itself that burden. And its failure of proof has been as abject as that of the debtor. To date the trustee has made only the vaguest suggestions as to how the debtor might be reorganized. It contends, however, that the proceedings should remain in federal court and urged both in the District Court and the Circuit Court of Appeals that this was desirable so that the securities could be subjected to "slow liquidation." Apparently the District Court was influenced in this direction because it said in its opinion that:

> "* * * The character of Debtor's assets is such that it would be peculiarly beneficial in its case to obtain slow and orderly liquidation, if such should be found to be the only feasible plan. The dumping upon the market of twenty million dollars worth of securities of the kind held in Debtor's portfolio would most certainly result in substantial losses, which may be avoided by slow and careful liquidation over an extended period of time. * * *" (R. 196-197)

A report filed in the District Court by the trustee on May 15, 1942, after the argument on appeal in the Circuit Court of Appeals, reveals that the trustee apparently no longer subscribes to this idea. The report is entitled "REPORT OF CENTRAL TRUST COMPANY, TRUSTEE, ON SECURITIES COMPRISING THE INVESTMENT PORTFOLIO OF FIDELITY ASSURANCE ASSOCIATION," and is printed at pp. 80 to 90 of the Appendix hereto. In this report it is said (App. 80):

> "Your Trustee further respectfully reports that all of the securities, excepting United States Treasury obligations and those rated 'A' or better, are regarded in the main by your Trustee as either falling in the so-

called 'marginal classification, or securities which cannot be regarded as satisfactory for investment of savings funds."

Each type of security is discussed and the conclusion reached that except for United States government bonds each and all of the securities comprising the state deposits should be promptly sold. In discussing state, county and municipal revenue bonds it is said (App. 82):

> "* * * The longer the delay in acting on such vulnerable securities, just to such an extent is the danger increased that satisfactory sale can be accomplished. * * *"

This is precisely in accord with the position these respondents took at the inception of the federal proceedings and with the position we take now. Nevertheless, the fact that Wisconsin had prior to the federal proceedings sold certain securities, comprising in large part municipal, railroad and industrial issues, was constantly pointed to both by the debtor and the trustee during the hearing in the District Court as having been an error and one of the chief reasons why the federal proceedings should continue. The only difference between the position which the trustee takes in its report filed May 15, 1942 and that of the respondents is that, instead of distributing the proceeds of the sales the trustee suggests that such proceeds shall be re-invested in securities of the trustee's choosing and retained by it. We can only conclude from the report that the trustee does not favor "slow and orderly liquidation" or see any purpose therein, and that it does favor speedy liquidation but *slow distribution*. The trustee apparently would do everything the states are seeking to do except to place the funds in

the hands of the contract holders who are entitled thereto. All that the trustee insists is that some plan (its nature undisclosed) shall be adopted whereby it shall have the control of the depositors' funds for an indefinite period of years. How the interests of contract holders are to be best subserved by such procedure, we cannot understand. The states emphatically disclaim any necessity for or intention of "dumping" the securities comprising the deposits on the market. See App. 26 for results of liquidation in Wisconsin.

Petitioners and the SEC suggest and have suggested an infinite number of legal questions which they conceive could arise between the state authorities and contract holders of the several states, and it is suggested that such questions should be decided in one forum.

The SEC brief advances the proposition that the state deposits may be found, after all, not to secure effectively the residents of the states for whose benefit the state deposit laws were enacted. They suggest that because of the manner in which Fidelity kept its books and because of certain provisions of the contracts, the securities which Fidelity placed on deposit with the states were impressed with a prior trust in its hands and therefore were improperly deposited with the states. Such a suggestion could hardly be heard to come from the debtor itself, whose petition is being tested in these proceedings, but in any event such speculations may be quickly disposed of. It is perhaps significant that while this question was raised frequently during the proceedings, particularly by counsel for the SEC, such counsel have consistently refused to make any positive statement as to their belief or disbelief in the theory that the state deposits were not valid as made. The District Court expressly stated that it made no determination of this point (R. 181).

The SEC brief states that when Fidelity deposited securities it made efforts to maintain segregation by series. It is then stated that "some of the state depositaries made their own selection of the securities to be deposited with them without regard to the particular fund of Fidelity to which the securities belonged." Such statements distort the record. The plain fact is, as is well known to everyone in these proceedings, that the state laws did not contemplate any segregation of securities by "funds" or "series," but merely that the securities on deposit should be of sufficient amount to secure the company's total liabilities in each particular state to the extent specified in the several laws, without regard to the fact that the company might from time to time develop and sell various "series" of contracts. And the state deposits were made on this theory during the entire life of the company. It was not until the SEC investigation in 1938 that suggestions began to be made that in some manner the securities were impressed with a trust by "funds" in the hands of the company. The great bulk of the deposits as presently constituted were made long prior to the SEC investigation. We refer to the joint statement of facts, *ante*, pp. 26 to 30, for a statement of the facts as to the various "funds" as related to the state deposits. The District Court expressly found (R. 181) that the debtor "made no attempt to proportion its deposits of securities from a particular fund to the amount of cash liabilities against that fund in the state where the securities were deposited." The Securities and Exchange Commission itself (as distinguished from its counsel) expressly found and reported to Congress that Fidelity's contracts were unsecured except for the state deposits (*ante*, pp. 28-30). And a reading of the contracts (Exs. 1-5, inclusive)

will make clear beyond all doubt that no trust was created thereby, it being expressly stated that the securities comprising the "reserves" were to be deposited "in trust as required by the laws of the State of West Virginia." The deposit law of West Virginia made provision for deposits in other states and the contracts sold in other states were, of course, subject to the provisions of the laws of such states. The trusts arose by virtue of the state laws and the deposits made thereunder and there are no other "trusts." The states, while assuming the validity of their laws, do not, as suggested by the SEC, attempt to preclude challenge thereof. The courts of Wisconsin and Iowa and of the other states are open to all who may desire on any theory to make claim against the funds on deposit there, and any questions so presented should be decided there.

The depositary states have worked in harmony during the entire course of these proceedings and should questions arise between them, we can see no reason for suggesting that they will not be determined in an expeditious and adequate manner.

It is probable that questions will arise as to who are proper claimants in any particular deposits and as to the proper measure of claims. And doubtless, there will be questions as to the relative rights of claimants in particular deposits. These are questions of state law.

Fischer v. American United L. Ins. Co., 314 U. S. 549, 86 L. ed. 444, 62 S. Ct. 380 (Jan. 1942);

American United L. Ins. Co. v. Fischer, 130 F. (2d) 643 (CCA 8th, July 1942).

Such questions of state law involve both the rights of contract holders within the states as to the funds on deposit there and the rights of the states and their lawfully consti-

tuted administrative bodies with respect to the regulation of the debtor's business within each of the several states.

These questions are not so formidable that the state courts cannot adequately cope with them. Assuming such questions to be complex and difficult their existence would not furnish any reason for extending the scope and purpose of Chapter X. In the liquidation of any large corporation doing business in a number of states and having pledged its property in various states under various laws, it is inevitable that a number of legal questions will arise. And such questions will arise whether the liquidation be conducted in state courts or in bankruptcy proceedings in the federal courts. This situation, however, did not lead Congress to extend the scope of the reorganization statute to supplant existing procedures, whether state or federal, for liquidation, nor will the exigencies of a particular case add to the federal court's jurisdiction under Chapter X.[1]

---

[1] In fact, the drafters of Chapter X considered this very question in rejecting the contention that insurance companies should be brought within the scope of the Act. A letter dated May 14, 1937 to Hon. Walter Chandler was introduced into the record of the hearing before the House Judiciary Committee, reading in part as follows:

"* * * Personally, I see no reason why insurance companies which fail should not be wound up in bankruptcy. As you know, most of these companies are operating in several States, necessitating separate receiverships or wind-ups in each State, with an enormous duplication in expenses and gross inequality of treatment between residents of various States. Sometimes, where one State happens to have a large amount of assets and another none, the policyholders are paid not on the basis of their claims prorating over the United States as a whole, but on the basis of what assets happen to be in their home State. I could give you many instances of cases where policyholders of one State are paid in full or paid a very large percentage of their claims, while at the same time policyholders of another State get little or nothing. By striking out the word 'insurance' in two places in the bill one very great abuse will be rectified."

Mr. Jacob Weinstein, one of the drafters of the bill, who appeared before the House Committee to explain its provisions, related to the Committee in reference to the letter:

"We have a letter from Mr. E. H. Elliott, an attorney of St. Louis, Mo. Mr. Elliott suggests that insurance companies be brought within the scope of corporate reorganizations. The conference has thoroughly canvassed and considered that whole subject of persons amenable to reorganization proceedings, and they have decided that in the case of insurance companies and banking corporations and the like, they be not brought within the scope of the reorganization proceedings. The cases of these companies, which are now excluded from the act—the various States have set up, first, controlling agencies in the operation of the companies; and, secondly, when companies become embarrassed, the agencies, in order to take care of them, and to liquidate them, when necessary; and it is the judgment of the conference that it would be much better to allow these companies to be liquidated or reorganized under local law, than to bring them in under the bankruptcy law. * * *"

P. 242, Hearing before Committee on the Judiciary, House of Representatives, 75th Cong., 1st Sess., on H. R. 6439.

Recent decisions of this court would indicate that were the federal proceedings to continue the District Court would be required to submit questions as to the construction of the deposit laws of the various states to the state courts of those states, where such questions had not yet been decided by the state courts.

Thompson v. Magnolia Petroleum Co., 309 U. S. 478, 84 L. ed. 876, 60 S. Ct. 628 (1940);

Railroad Commission of Texas v. Pullman Co., 312 U. S. 496, 85 L. ed. 971, 61 S. Ct. 643 (1941), *infra*;

Fischer v. American United L. Ins. Co., 314 U. S. 549, 86 L. ed. 444, 62 S. Ct. 380 (1942).

If, in any event, the federal court would be required to refer such matters to the state courts for disposition, it seems unreasonable to suggest that a multiplicity of state court actions can be avoided by an assumption of federal jurisdiction. On the contrary, it clearly appears that such assumption of jurisdiction would result in the addition of yet another court to those which must ultimately pass upon the questions at issue. Common sense dictates that where the important questions in the case must be referred to the state courts in any event, each of those courts should be permitted to effect a complete disposition of the deposits in their respective states.

III

THE PUBLIC INTEREST, UNDER WELL SETTLED EQUITY PRINCIPLES APPLICABLE IN CHAPTER X PROCEEDINGS, REQUIRED DISMISSAL OF THE PETITION BY THE DISTRICT COURT

Equitable principles applicable in Chapter X proceedings required dismissal of the petition by the District Court. These principles may be considered as existing independently of the express words of Chapter X or as an aspect of the question of "good faith" within the general meaning of that term as used in Chapter X.

We advanced this contention before the Circuit Court of Appeals, and it is open here.

Ryerson v. United States, 312 U. S. 405, 85 L. ed. 917, 61 S. Ct. 656 (1941).

Section 77B and Chapter X were and are but an extension and codification of the rules of law and practice which had been developed in the former federal equity receivership proceedings.

Finletter, Law of Bankruptcy Reorganization (1939 ed.), pp. 1-35, particularly pp. 18-19.

This proposition is explained in the fullest of detail in *Securities and Exchange Commission v. United States R. & Imp. Co.*, 310 U. S. 434, 84 L. ed. 1293, 60 S. Ct. 1044 (1940). The question there was whether, even though it be conceded that jurisdiction to entertain the debtor's petition existed under Chapter XI of the Bankruptcy Act, the District Court should have proceeded under Chapter X on the ground that such procedure was better adapted to the circumstances of the case. It was held that even though

Chapter XI did not contain in words provisions similar to Section 146 of Chapter X, the District Court should in the exercise of sound discretion have dismissed the Chapter XI petition and remitted respondent, if it was so advised, to the initiation of a proceeding under Chapter X. During the discussion it was said:

> "A bankruptcy court is a court of equity, § 2, 11 USCA § 11, and is guided by equitable doctrines and principles except in so far as they are inconsistent with the Act. * * *" (310 U. S. 455)

We direct particular attention to the citation and discussion of the case of *Pennsylvania v. Williams*, 294 U. S. 176, 79 L. ed. 841, 55 S. Ct. 380 (1935), in the *United States R. & Imp. Co.* case. In citing that case it was said:

> "* * * A court of equity may in its discretion in the exercise of the jurisdiction committed to it grant or deny relief upon performance of a condition which will safeguard the public interest. It may in the public interest, even withhold relief altogether, and it would seem that it is bound to stay its hand in the public interest when it reasonably appears that private right will not suffer. * * *" (310 U. S. 455)

There can be no question but that the principles of *Pennsylvania v. Williams* and related cases are imported into the application of Chapter X.

In *Pennsylvania v. Williams*, 294 U. S. 176, 79 L. ed. 841, 55 S. Ct. 380 (1935), a federal District Court had appointed an equity receiver of a Pennsylvania building and loan association. Later, the appropriate authorities of Pennsylvania had intervened and moved for dismissal upon the ground that the statutes of Pennsylvania afforded a com-

plete scheme for liquidation of the association. It was held to be error for the District Court to have retained jurisdiction. It was said:

"* * * It is in the public interest that federal courts of equity should exercise their discretionary power with proper regard for the rightful independence of state governments in carrying out their domestic policy. (citing) It has long been accepted practice for the federal courts to relinquish their jurisdiction in favor of the state courts, where its exercise would involve control of or interference with the internal affairs of a domestic corporation of the state. (citing) There are stronger reasons for adopting a like practice where the exercise of jurisdiction involves an unnecessary interference by injunction with the lawful action of state officers. (citing)" (294 U. S. 185)

See also: *Gordon v. Ominsky*, 294 U. S. 186, 79 L. ed. 848, 55 S. Ct. 391 (1935);

Penn General Casualty Co. v. Pennsylvania, 294 U. S. 189, 79 L. ed. 850, 55 S. Ct. 386 (1935);

Kelleam v. Maryland Casualty Co., 312 U. S. 377, 85 L. ed. 899, 61 S. Ct. 595 (1941);

Annotation, 96 A. L. R. 1173.

As said in *Railroad Commission of Texas v. Pullman Co.*, 312 U. S. 496, 85 L. ed. 971, 61 S. Ct. 643 (1941):

"* * * Few public interests have a higher claim upon the discretion of a federal chancellor than the avoidance of needless friction with state policies, whether the policy relates to the enforcement of the criminal law, Fenner v. Boykin, 271 U. S. 240, 70 L. ed. 927, 46 S. Ct. 492; Spielman Motor Sales Co. v. Dodge, 295 U. S. 89, 79 L. ed. 1322, 55 S. Ct. 678; or the administration of a specialized scheme for liquidating embar-

rassed business enterprises, Pennsylvania v. Williams, 294 U. S. 176, 79 L. ed. 841, 55 S. Ct. 380, 96 A. L. R. 1166; or the final authority of a state court to interpret doubtful regulatory laws of the state, Gilchrist v. Interborough Rapid Transit Co. 279 U. S. 159, 73 L. ed. 652, 49 S. Ct. 282; cf. Hawks v. Hamill, 288 U. S. 52, 61, 77 L. ed. 610, 618, 53 S. Ct. 240. These cases reflect a doctrine of abstention appropriate to our federal system whereby the federal courts, 'exercising a wise discretion,' restrain their authority because of 'scrupulous regard for the rightful independence of the state governments' and for the smooth working of the federal judiciary. See Cavanaugh v. Looney, 248 U. S. 453, 457, 63 L. ed. 354, 358, 39 S. Ct. 142; Di Giovanni v. Camden F. Ins. Asso., 296 U. S. 64, 73, 80 L. ed. 47, 53, 56 S. Ct. 1. This use of equitable powers is a contribution of the courts in furthering the harmonious relation between state and federal authority without the need of rigorous congressional restriction of those powers. * * *" (312 U. S. 500-501)

The statutes of Pennsylvania providing for the liquidation of building and loan associations are substantially identical to the statutes of Wisconsin which cover the proceedings there in this case. An even more striking application of these principles as applied to the facts of this case was made in *Brashear v. Intermountain Building & Loan Ass'n*, 109 F. (2d) 857 (CCA 9th, 1940), and in *Gallegos v. Smith*, 111 F. (2d) 805 (CCA 9th, 1940). In these latter cases the corporation, as here, had deposits in various states and the state authorities had proceeded precisely as they have done here and under statutes substantially similar.

To propose in this case that the lawful functions of the state authorities shall be suspended, the contract holders in the several states deprived of all assistance therefrom

and to relegate them to pursuance of their own remedies in a far-off federal District Court, is to flout the states and the very laws under which the contract holders assumed their relationship with the debtor, upon which they rely for the fulfillment of its obligations, and to which the debtor owed its life and business.

In their function as liquidators of insolvent financial institutions over which they have control, the Banking Commissioners of Wisconsin "are executive or administrative officers carrying out a legislative policy." *Pallange v. Liberty State Bank*, 216 Wis. 418, 421, 256 N. W. 708, 710. The states' conception of their position and duty is expressed better than we are able to do in the opinion by Mr. Justice Cardozo in *Hopkins Federal Savings and Loan Association v. Cleary*, 296 U. S. 315, 80 L. ed. 251, 56 S. Ct. 235 (1935) (cited in *Securities and Exchange Commission v. United States R. & Imp. Co.*):

> "The standing of Wisconsin to resist a trespass on its powers is confirmed if we view the subject from another angle of approach. In the creation of corporations of this quasi-public order and in keeping them thereafter within the limits of their charters, the state is parens patriae, acting in a spirit of benevolence for the welfare of its citizens. Shareholders and creditors have assumed a relation to the business in the belief that the assets will be protected by all the power of the government against use for other ends than those stated in the charter. Aside from the direct interest of the state in the preservation of agencies established for the common good, there is thus the duty of the parens patriae to keep faith with those who have put their trust in the parental power. * * *" (296 U. S. 340-341)

CONCLUSION

It is respectfully submitted that the judgment of the Circuit Court of Appeals should be affirmed.

JOHN E. MARTIN,
Attorney General, State of Wisconsin,

JAMES WARD RECTOR,
Deputy Attorney General, State of Wisconsin,

RICKARD H. LAURITZEN,
Assistant Attorney General, State of Wisconsin,

Attorneys for Respondent,
Banking Commission of Wisconsin.

JOHN M. RANKIN,
Attorney General, State of Iowa,

FLOYD PHILBRICK,
First Assistant Attorney General, State of Iowa,

CARL J. STEPHENS,
BEN C. BUCKINGHAM,

Attorneys for Respondent,
Charles R. Fischer, Commissioner of Insurance and Permanent Receiver for Debtor Corporation In and For the State of Iowa.

APPENDIX

APPENDIX TABLE OF CONTENTS

APPENDIX

1

STATUTES OF WISCONSIN, INSOFAR AS PERTINENT TO THE ISSUES IN THIS CASE, TO WHICH FIDELITY ASSURANCE ASSOCIATION WAS AND IS SUBJECT

Chapter 216

Investment Associations

216.01 Regulation. No person and no copartnership, association or corporation, whether local or foreign, heretofore organized or which may hereafter be organized, doing business as a so-called investment, loan, benefit, cooperative, home, trust or guarantee company, for the licensing, control and management of which there is no law now in force in this state, and which such person, copartnership, association or corporation, shall solicit payments to be made to himself or itself either in a lump sum, or periodically, or on the instalment plan, issuing therefor so-called bonds, shares, coupons, certificates of membership or other evidences of obligation or agreement, or pretended agreement to return to the holder or owners thereof money or anything of value at some future date, shall solicit or transact any business in this state unless such person, copartnership, association or corporation, shall have first complied with all the provisions prescribed in chapter 215 of the statutes required of foreign building and loan associations authorized to do business in this state.

216.02 Laws applicable. All provisions of said chapter 215 with respect to the supervision, control and conditions upon which foreign building and loan associations are permitted to do business in this state are hereby made applicable to and imposed upon persons, copartnerships, associations or corporations described in the first section of this act, the same as though they were foreign building

and loan associations under said act, so far as such supervision, control and conditions can be made applicable to the particular business done by such persons, copartnerships, associations or corporations.

216.03 Penalty. Any person, copartnership, association or corporation who or which shall act as principal or agent in doing such business or in soliciting business for, or membership of participation in, any such copartnership, association or corporation, or solicit business for such person or persons doing business as such companies, not authorized to do business in this state, shall be deemed guilty of a misdemeanor and upon conviction thereof shall be punished by fine of not less than one hundred dollars nor more than one thousand dollars, or by imprisonment in the county jail of not less than three months, nor more than one year, or by both such fine and imprisonment.

(Secs. 216.04 to end of Chapter 216 omitted.)

Chapter 215

Building and Loan Associations

215.01 Local and foreign; organization. (1) A corporation for the purpose of raising money to be loaned among its members shall be known as a building and loan association; if organized under the laws of this state, as a local association, and if under the laws of any other state or territory, as a foreign association. The words "building and loan association" shall form part of the name of every such local association hereafter organized; and no corporation not organized under these statutes shall be entitled to use a name embodying such words, except that corporations now existing may continue their present names. The

name adopted by any association hereafter incorporated shall not be the same assumed by any other association, nor so similar as to be liable to mislead.

215.38 **Deposit.** No foreign building and loan association and no foreign association or corporation representing itself to be a building and loan association or doing business on the building-society plan, and no association or corporation organized under the laws of any other state or territory and doing business in the manner provided for mutual loan and building associations by this chapter shall issue its shares, receive moneys or transact any business in this state unless such association shall have and keep on deposit with the state treasurer, in trust for the benefit and security of all its members in this state, five hundred thousand dollars to be held in trust as aforesaid until all shares of such association held by residents of this state shall have been fully redeemed and paid off and until its contracts and obligations to persons and members residing in this state shall have been fully performed and discharged; the securities comprising such deposit shall first be approved by the banking commission under the same rules and regulations governing the approval of securities of trust company banks; and upon such deposit being made the state treasurer shall issue a certificate therefor, and thereupon the banking commission may issue its certificate of authority to said association to transact business in this state.

215.39 **Same.** The deposit to be made with the state treasurer by any foreign association may consist of bonds or treasury notes of the United States, or bonds of this state or any city, town or county of this state, having authority to issue the same. All interest which may accrue on securities held by the state treasurer may be collected, and retained by the association depositing such securities so long as such association remains solvent and performs all

contracts with its members. Any securities on deposit as provided herein, if approved by the banking commission, may from time to time be withdrawn if others of equal value and of the character named in this section are substituted therefor. If any such securities shall depreciate in value new ones must be added, so that the deposit may at all times be kept good and of the value of five hundred thousand dollars, and it shall be the duty of the banking commission to revoke the certificate of authority of any such association whenever there exists an impairment of such deposit for a period of more than thirty days after due notice to the association given by such commission.

215.395 **Increase of deposit.** Whenever the commission shall find that the liability of any foreign building and loan association or any foreign investment association on shares or contracts then outstanding or contracted for by members or persons residing in this state, exceeds ninety per cent of the amount of the deposit required by section 215.38 and section 215.39, or exceeds ninety per cent of the amount of the deposit required by such sections and by any order issued under the authority of this section, exclusive in each case, however, of any such liability under any agreement existing, created, regulated or required by the industrial commission under chapter 108 or by any other department, commission or division of a state government under any other provision of law, the commission shall issue an order to such association or corporation requiring such association or corporation to deposit within thirty days with the state treasurer, an additional amount in cash or securities of the class mentioned in section 215.39, or such other securities as the commission shall require and approve. If such order is not complied with within thirty days, the commission shall revoke the certificate of authority issued to such association or corporation.

215.41 **Conditions precedent.** Every foreign building and loan association, before commencing to do business in this state, shall:

(1) File with the banking commission a duly authenticated copy of its charter or articles of incorporation and by-laws, of its certificates of shares and of all printed matter issued by it.

(2) File with the banking commission a certificate of the state officer having charge and supervision of such associations in the state in which incorporated, certifying that such association is legally incorporated and authorized to transact business, and that similar associations incorporated under the laws of this state are permitted and licensed to transact business in such state.

(3) Pay to the banking commission one hundred dollars for filing the papers mentioned in this section. Before granting a license to any such association organized or incorporated under the laws of any other state or foreign government it shall require that every such association shall file in writing an appointment of the banking commission or its successor in office as the attorney upon whom any summons, notice or process of any court of this state may be served and stipulate that service of any such summons, notice or process upon such attorney, in any action brought upon any cause of action arising out of any business or transaction in this state, shall be accepted irrevocably as a valid service upon such association, and copies of said appointment, certified by the banking commission, shall be deemed sufficient evidence of its authority to accept service as the attorney on behalf of any such association. Each such association shall agree, in such appointment of attorney, that the license granted by the banking commission shall cease and be revoked in case such association shall remove or make application to remove into any court of the United States any action or proceeding commenced

in any court of this state upon a claim or cause of action arising out of any business or transaction done in this state, and it shall be the imperative duty of the banking commission to revoke any and every authority, license or certificate granted to any such association violating the provisions of this section, and no such association shall have its license or certificate of authority renewed for three years after such revocation, and shall agree that in the event of revocation of license such appointment of the banking commission shall continue for the purpose of serving process for beginning actions upon any certificate of stock or liability incurred or contracted in this state while it transacted business therein, so long as any liability shall exist. When legal process against any such association is served upon the banking commission, it shall immediately notify the association of such service by letter and inclose a copy of the process served on it to said association or to any person designated by the officers thereof in writing. The plaintiff, for each process so served, shall pay to the banking commission, or, at the time of such service, a fee of two dollars, which shall be recovered by the plaintiff as a part of the taxable costs if it prevail in the suit. The banking commission shall keep a record of all process served on it, which record shall show the day and hour when such service was so made, and all the fees received by it on account of the service of such process shall be paid into the state treasury.

215.45 Agents; fee. No person shall act as the agent or representative of any foreign building and loan association until after he shall, at the request of such association, have procured from the banking commission a license reciting the fact that such association is authorized and licensed to transact business in this state and has complied with all lawful requirements. The fee for such license shall be twenty-five dollars, and the license shall continue in

force, unless sooner revoked by the commission, during and until the close of the fiscal year of the association.

215.46 . Withdrawing securities. Any foreign building and loan association, having made the deposit of securities required by this chapter, and desiring to withdraw the same or any of them without depositing securities of like character and amount, or desiring to discontinue its business or withdraw from the state, may do so by complying with the following provisions: File with the banking commission a statement reciting the reasons for desiring to withdraw such securities and the amount to be withdrawn; and the commission shall thereupon examine such association and determine the amount of its liabilities on account of all agreements or contracts outstanding with residents of this state, and if convinced that the interests of such residents will not be injured or jeopardized by such withdrawal shall cause to be published in three newspapers in this state for three weeks, at the expense of the association, notice of such request for the withdrawal of such securities, and if no written objection is filed by any resident of this state holding any share, certificate, bond or other evidence of indebtedness of or against such association within one week after the last date of the publication of such request the banking commission shall issue a certificate certifying to the state treasurer the amount of liabilities, if any, existing in this state and the amount of securities such association shall be permitted to withdraw, and upon filing a receipt for such amount the association shall be permitted to withdraw the same; provided, that there shall remain at all times a sufficient deposit to protect residents of this state holding shares, certificates, bonds or other evidences of indebtedness of or against such association and that such deposit shall decrease only as the liabilities of such association decrease on account of such residents.

215.33 Possession by banking commission. (1) CONDITIONS FOR TAKING POSSESSION. The banking commission may forthwith take possession and control of the business and property of any association to which this chapter is applicable whenever it shall find that such association:

(a) Is conducting its business contrary to law, or,

(b) Has violated its charter, or any law, or

(c) Is conducting its business in an unauthorized or unsafe manner, or

(d) Is in an unsound or unsafe condition to transact its business, or

(e) Has an impairment of its capital, or

(f) Cannot with safety and expediency continue business, or

(g) Has suspended payment of its obligations, or

(h) Has neglected or refused to comply with the terms of a duly issued order of the commission, or

(i) Has refused to submit its books, papers, records, or affairs for inspection to any examiner, or

(j) Has refused to be examined upon oath regarding its affairs.

(2) PROCEDURE ON TAKING POSSESSION. Upon taking possession of the business and property of any such association the banking commission shall forthwith:

(a) Serve a notice in writing upon the president and secretary of said association, setting forth therein that it has taken possession and control of the business and property of said association. Said notice shall be executed in duplicate, and immediately after the same has been served, one of the said notices shall be filed with the clerk of the circuit court of the county where said association is located, together with proof of service.

(b) Give notice to all individuals, partnerships, corporations and associations known to the banking commis-

sion to be holding or in possession of any assets of such association.

(c) The banking commission may appoint one or more special deputy commissioners as agent or agents to assist in the duty of liquidation and distribution of the assets of one or more building and loan associations of whose business and property the banking commission shall have taken possession pursuant to the provisions of this chapter. A certificate of such appointment shall be filed in the office of the banking commission and a certified copy in the office of the clerk of the circuit court for the county in which such building and loan association is located. The banking commission may employ such counsel and procure such expert assistance and advice as may be necessary in the liquidation and distribution of the assets of such building and loan associations, and may retain such of the officers or employes of such building and loan associations as they may deem necessary. The special deputy commissioner and assistants shall furnish such security for the faithful discharge of their duties as the banking commission deems proper. Such special deputy commissioner may execute, acknowledge and deliver any and all deeds, assignments, releases or other instruments necessary and proper to effect any sale and transfer or incumberance of real estate or personal property and may borrow money for use in the liquidation after the same has been approved by the banking commission, and an order obtained from the circuit court of the county in which said association is located, as hereinafter provided.

(d) Upon taking possession of the property and business of such building and loan association, the special deputy commissioner of banking is authorized to collect all moneys due to such building and loan association, and do such other acts as are necessary to conserve its assets and business, and shall proceed to liquidate the affairs thereof

as hereinafter provided. He shall collect all debts due and claims belonging to it, and upon a petition approved by the banking commission and upon order of the circuit court of the county in which such association is located, may sell or compound all bad or doubtful debts, or do any act or execute any other necessary instruments and upon like petition and order may sell all the real and personal property of such building and loan association on such terms as the court shall approve. Such special deputy commissioner may, if necessary, enforce individual liability of the stockholders to pay the debts of such corporation.

(e) The banking commission may, in the event of its taking possession of any building and loan association, the shares or share accounts of which are to any extent insured by the federal savings and loan insurance corporation, tender to said corporation the appointment as statutory liquidator of such association. If it does not make such tender it shall tender to said federal savings and loan insurance corporation the appointment as statutory coliquidator of such association to act jointly with the banking commission, but such coliquidatorship shall not extend over a period of more than one year from the date of such tender, at the expiration of which time the banking commission shall become the sole liquidator except as herein otherwise provided. The commission shall tender to said corporation the appointment as sole statutory liquidator of such association whenever said corporation shall have become subrogated to the rights of at least 90 per cent of the outstanding liability of such association on shares and share accounts; and if in addition said corporation shall have deposited with the clerk of the circuit court for the county in which such association is located shares or share accounts in a local insured association not in default at least equal in amount to the shares and share accounts as to which the corporation has not become subrogated, or if the corporation shall become

subrogated as to all the shares and share accounts in such association, it may then exercise all the powers and privileges herein conferred upon it without court order or approval. It shall be the duty of such clerk to accept such deposit for the benefit of the persons entitled to such shares or share accounts.

(f) If said corporation accepts such appointment as sole liquidator it shall have and possess all the powers and privileges given by the laws of this state to the banking commission as statutory liquidator of a possessed building and loan association, as provided in section 215.33 or otherwise, including section 215.116 and be subject to all the duties of the banking commission as such statutory sole liquidator, except in so far as such powers, privileges or duties are in conflict with the provision of any applicable federal laws, and except as herein otherwise provided, unless and until such association shall resume business, pursuant to subsection (11) or subsection (12) of section 215.33. If said corporation accepts such appointment as coliquidator it shall have and possess such powers and privileges equally and jointly with the banking commission and shall be subject to such duties equally and jointly with said commission.

(g) In the event said federal savings and loan insurance corporation shall accept the appointment as such coliquidator or liquidator, it shall file such acceptance with the banking commission and the clerk of the circuit court of the county in which the association is located and it is authorized and empowered to be and act, without bond, as such coliquidator or liquidator. Upon the filing by said federal savings and loan insurance corporation of its acceptance of the appointment as such sole liquidator, the possession of and title to all the assets, business and property of such association of every kind and nature shall pass to and vest in said corporation without the execution of any instru-

ments of conveyance, assignments, transfer or indorsement. Upon the filing by said corporation of its acceptance of the appointment as coliquidator such possession and title shall pass to and be vested in the banking commission and said corporation jointly. In the event said corporation shall not qualify as sole liquidator at or before the time herein provided for the expiration of such coliquidatorship, said corporation shall be wholly divested of and from such joint title and possession and the sole title and possession shall thereupon vest immediately in the banking commission. The vesting of title and the possession of the property and assets of such association, as provided by subsection (8) of section 215.33, shall not render such property or assets subject to any claims or demands against the federal savings and loan insurance corporation, except such as may be incurred by such corporation with respect to such association and its property or assets. Whether or not it shall serve as aforesaid, the federal savings and loan insurance corporation may make loans on the security of or may purchase, with the approval of the court, except as herein otherwise provided, at public or private sale, all or any part of the assets of any association, the shares, share accounts or accounts of which are to any extent insured by it, but in the event of such sale and purchase, said corporation shall bid for and pay a fair and reasonable price.

(h) Whether or not said federal savings and loan insurance corporation shall serve as liquidator of any such association, whenever it shall pay or make available for payment the shares, share accounts or accounts of any such association in liquidation which are insured by it, it shall be subrogated upon the surrender and transfer to it of any such shares, share accounts or accounts, with respect to such shares, share accounts or accounts, but such surrender and transfer shall not affect any right which the transferor may have in any portion of such shares, share accounts or

accounts which are not paid or made available for payment, or any right to participate in the distribution of the net proceeds remaining from the disposition of the assets of such association; provided, that the rights of the investors and creditors of such association shall be determined in accordance with the applicable provisions of the laws of this state.

(3) NOTICE, ALLOWANCE AND PAYMENT OF CLAIMS. The special deputy commissioner of banking shall cause notice to be given by advertisement in such newspapers as he may direct, weekly, for 3 consecutive weeks, calling on all persons who may have claims against such building and loan association, to present the same to the special deputy commissioner of banking, and make legal proof thereof at a place and within a time, not earlier than the last day of publication, to be therein specified. He shall mail a similar notice to all persons at their last known address, whose names appear as creditors upon the books of the building and loan association. Proof of service of such notice shall be filed with the clerk of said court. The special deputy commissioner may reject any claim. Any party interested may also file written objections to any claim with the special deputy commissioner of banking and after notice by registered mail of such rejection, said claimant shall be barred unless he commences an action thereon within 3 months. Claims presented after the expiration of the time fixed in the notice to creditors shall be entitled to share in the distribution only to the extent of the assets then in the hands of the special deputy commissioner of banking equitably applicable thereto.

(4) INVENTORY OF ASSETS AND STATEMENT OF LIABILITIES. Upon taking possession of the property and assets of such building and loan association, the special deputy commissioner of banking shall make an inventory of the assets of such building and loan association, in duplicate, one to be

filed in the office of the banking commission, and one in the office of the clerk of circuit court for the county in which such building and loan association is located. Upon the expiration of the time fixed for the presentation of claims, the special deputy commissioner of banking shall make in duplicate a full and complete list of the claims presented, including and specifying such claims as have been rejected by him, one to be filed in the office of the banking commission, and one in the office of the clerk of circuit court for the county in which such building and loan association is located. Such inventory and list of claims shall be open at all reasonable times to inspection.

(5) ADJUSTMENT OF LOANS AND WITHDRAWAL VALUE OF SHARES. The value of shares pledged upon a loan to such association shall be applied and credited to such loan and the borrower shall be liable only for the balance. The rate of interest charged upon such balance shall be the legal rate. The value shall be determined in such manner as the banking commission prescribes, and shall be made pursuant to subsections (1) and (3) of section 215.332, or in such other manner as the banking commission may prescribe. Upon the approval of such value by the banking commission and the circuit court of the county in which such building and loan association is located, the book value of each member shall be reduced proportionately. At least 5 days' written notice of such determination of value shall be given to all shareholders of the time and place such value shall be submitted to the circuit court for approval. Should any stockholder or creditor of such association feel aggrieved by any such determination of value, he may at any time within 15 days after the mailing of a notice by the banking commission, addressed to the last known address of such party, giving notice of such determination and value of such shares, appeal to the supreme court. After the creditors of such association shall have been paid, the associa-

tion, and the members thereof, may avail themselves of the provisions of section 215.116.

(6) COMPENSATION AND EXPENSES IN CONNECTION WITH LIQUIDATION. The compensation of the special deputy commissioners, counsel and other employes and assistants, and all expenses of supervision and liquidation shall be fixed by the banking commission, subject to the approval of the circuit court for the county in which such building and loan association is located, and shall upon the certificate of the banking commission be paid out of the funds of such building and loan association. Expenses of supervision and liquidation shall include the cost of the service rendered by the building and loan division of the banking department to the building and loan association being liquidated and shall be determined from time to time by the banking commission and shall be paid to the banking department from the assets of the building and loan association as other expenses of liquidation are paid. The moneys collected by the special deputy commissioner of banking shall be from time to time deposited in one or more state banks, and, in case of the suspension or insolvency of the depository, such deposits shall be preferred before all other deposits.

(7) DIVIDENDS. At any time after the expiration of the date fixed for the presentation of claims, the special deputy commissioner of banking in charge of the liquidation of such building and loan association may, upon a petition approved by the banking commission and an order of the circuit court of the county in which such building and loan association is located, out of the funds remaining, after the payment of expenses and debts, declare one or more dividends, and may declare a final dividend, such dividend to be paid to such persons, and in such amounts as may be directed by the circuit court.

(8) TITLE PASSES TO BANKING COMMISSION. Immediately upon filing the notice as provided for in subsection (2)

of section 215.33, the possession of all assets and property of such building and loan association of every kind and nature, wheresoever situated, shall be deemed to be transferred from such association to, and assumed by the banking commission; and filing of the notice mentioned herein, shall of itself, and without the execution or delivery of any instruments of conveyance, assignment, transfer or indorsement, vest the title to all such assets and property in the banking commission. Such filing shall also operate as a bar to any attachment, garnishment, execution or other legal proceedings against such building and loan association, or its assets and property, or its liabilities.

(9) EFFECT OF POSSESSION. No building and loan association shall have a lien, or charge for any payment, advance or clearance made, or liability thereafter incurred, against any of the assets of the building and loan association of whose property and business the banking commission shall have taken possession.

(10) APPEAL. Whenever any such building and loan association whose property and business the banking commission has taken possession of, as aforesaid, deems itself aggrieved thereby, it may, at any time within ten days after such taking, apply to the circuit court of Dane county to enjoin further proceedings; and said court after citing the banking commission to show cause why further proceedings should not be enjoined and hearing all allegations and proofs of the parties and determining the facts, may, upon the merits dismiss such application or enjoin the banking commission from further proceedings, and direct it to surrender such business and property to such building and loan association.

(11) REINSTATEMENT. Whenever the banking commission shall have taken over the possession and control of the business and property of any building and loan association, the same may resume business when and if:

(a) The owners of at least two-thirds of such association's dollar value of outstanding shares, execute a petition to such effect, the form of which shall be prescribed by the banking commission, and

(b) There is submitted to the banking commission by such shareholders or a committee duly selected by them, a plan for the reorganization and reinstatement of such association, and

(c) The banking commission recommends that control of the business and property of such association be returned to the shareholders, and

(d) The court in which such liquidation is pending, upon application of the banking commission, makes an order approving the banking commission recommendations, which order shall contain a finding that such association will be in a safe and sound condition when control is resumed by the shareholders.

(12) REINSTATEMENT UPON RESTRICTED BASIS. Such building and loan association may also resume business upon a restricted basis, and upon such limitations and conditions as may be prescribed by the banking commission when approved by the circuit court in and for the county in which such building and loan association is located, upon application of the banking commission. Such restrictions and conditions may include, among others, a prohibition against the selling of new shares, reasonable restrictions upon withdrawals and the payment of other liabilities. Such association shall thereupon be relieved from the control and supervision of the banking commission as provided in this section, but nothing herein shall, in any manner, prohibit the banking commission from again proceeding against such association as provided herein.

(13) LIQUIDATING DIVIDENDS AND UNCLAIMED FUNDS. (a) Unclaimed liquidating dividends and unclaimed funds remaining unpaid in the hands of the special deputy com-

missioner of banking for six months after the order for final distribution shall be by him deposited in one or more state banks, to the credit of the banking commission in its name, in trust for the several shareholders and creditors. The banking commission shall include in its annual report to the governor the names of building and loan associations so taken possession of and liquidated, and the sums of unclaimed and unpaid liquidating dividends and unclaimed funds with respect to each of them respectively, including a statement of interest earned upon such funds.

(b) The banking commission may pay over the moneys so held by it to the persons respectively entitled thereto, upon being furnished satisfactory evidence of their right to the same. In case of doubt or conflicting claims, it may require an order of the circuit court authorizing and directing the payment thereof. It may apply the interest earned by the moneys so held by it towards defraying the expenses in the payment and distribution of such unclaimed liquidating dividends and funds to the stockholders and creditors entitled to receive the same.

(Other portions of Chapter 215 omitted as not pertinent.)

Chapter 189

Securities Law

189.12 Limitation of sales. No person shall sell or offer for sale in this state any security unless registered under section 189.13; • • •

189.13 Registration of securities. (1) Securities shall be registered under this chapter upon application and in the manner provided in this section.

(2) The application for registration shall be signed by the issuer or a licensed dealer, shall be verified and shall be filed with the department. It shall contain such information and representations as the department may require as necessary or appropriate in the public interest or for the protection of investors.

(3) The department shall examine such application and the other papers and documents filed therewith, and may make or have made a detailed inspection, appraisal, audit, or other investigation of the property and affairs of the issuer. The department, upon payment of the expense reasonably attributable to its investigation, shall by order register the securities covered by such application if the following shall be made to appear to the department:

(a) The proposed plan of business of the issuer is not unlawful, dishonest, fraudulent, or otherwise contrary to public policy.

(b) The plan of financing is not or does not tend to be unfair, inequitable or fraudulent, or against public interest or the interest of investors.

(c) The articles of incorporation or association, declaration of trust, charter, constitution, by-laws, lease, contract, or any instrument or indenture under which the securities are issued is not contrary to law or unfair, inequitable, or fraudulent.

(d) The class of securities for which registration is sought bears a reasonable proportion to other classes of securities and to the fair value of the property and business, due consideration being given to the nature of the business, its earnings, its credit and propects, the possibility that the fair value of the property and business may change from time to time, the effect which the issue of such securities may have on the management and operation of the business by reason of the relative amount of finan-

cial interest which the various classes of security holders will have in the business, and to other relevant matters.

(e) The commissions, fees and expenses to be incurred in connection with such issue or the sale thereof or the gross or net profit of any party or parties in connection therewith, is not unreasonable.

(f) The advertising matter to be used in the sale of the securities is not false, unfair, inequitable, fraudulent or misleading and gives fair and reasonably adequate information with reference to the securities and the issuer.

(g) It does not appear that any relationship exists between the issuer and the trustee in any instrument under which the securities have been or are to be issued, by virtue of which the interests of the trustee might be in conflict with the interests of purchasers.

(h) The methods to be used in the sale of the securities are not such as to be misleading, unfair, inequitable or fraudulent as to the purchasers, or against public interest or the interest of investors. Unless the foregoing shall be made to appear to the department, the department shall issue its findings and order denying registration.

(Other portions of Chapter 189 omitted as not pertinent.)

NOTICE OF TAKING CONTROL OF WISCONSIN BUSINESS AND PROPERTY OF FIDELITY ASSURANCE ASSOCIATION

(From Ex. 120)

(Caption Omitted)

To: Fidelity Assurance Association
Wheeling, West Virginia

F. S. Risley, President
Fidelity Assurance Association
Wheeling, West Virginia

Frank J. McNulty, Vice President and Secretary
Fidelity Assurance Association
Wheeling, West Virginia

H. Isaiah Smith
Ross B. Thomas
Receivers of Fidelity Assurance Association
Charleston, West Virginia

PLEASE TAKE NOTICE:

That the Banking Commission of Wisconsin, acting pursuant to the provisions of Chapter 216 and Chapter 215, Wisconsin Statutes, particularly section 215.33 thereof, and pursuant to the order of the Circuit Court for Dane County made and entered on April 14, 1941, has taken possession and control of all of the business and property located in the State of Wisconsin of Fidelity Assurance Association.

This notice, executed this 26th day of April, 1941.

BANKING COMMISSION OF WISCONSIN

By Frank H. Bixby /s/
Frank H. Bixby
Commissioner of Banking

(SEAL)

ORDER OF CIRCUIT COURT FOR DANE COUNTY, WISCONSIN, APRIL 14, 1941

(From Ex. 120)

(Caption Omitted)

On reading and filing the petition of the Banking Commission of Wisconsin dated April 14, 1941, and said Commission appearing by Frank H. Bixby, Commissioner of Banking; John E. Martin, Attorney General; and Rickard H. Lauritzen, Assistant Attorney General; and said Fidelity Assurance Association appearing by its attorneys Rieser and Mathys by R. M. Rieser, and the Court being advised as to the nature and purpose of the petition, and being satisfied that the petition sets forth facts sufficient to support an order to be entered herein, and that facts exist establishing the jurisdiction of the Court and that it is necessary and desirable that an order be promptly entered herein;

NOW, THEREFORE, IT IS ORDERED:

1. That possession and control of all of the property, business and assets of Fidelity Assurance Association, a corporation organized and existing under the laws of the State of West Virginia, located in the State of Wisconsin of whatever nature and wherever located in the State of Wisconsin be and the same hereby is vested in the Banking Commission of Wisconsin; and said Commission is hereby ordered to forthwith take possession of and hold said property, said property to be administered by the Banking Commission of Wisconsin under the supervision and con-

trol of the Circuit Court for Dane County, Wisconsin, for the benefit and security of contract, bond or certificate holders, residents of this State, and other creditors of said Association located in Wisconsin.

2. That title to the securities heretofore deposited by said Fidelity Assurance Association with the State Treasurer of Wisconsin as set forth in said petition, being securities having a market value as of February 28, 1941, as set forth in said petition, of $2,606,883.16, and interest coupons appertaining thereto in the amount of $28,394.53, likewise on deposit with the State Treasurer of Wisconsin, in trust for the benefit and security of Wisconsin contract, bond or certificate holders and creditors, be likewise vested in the Banking Commission of Wisconsin, custody and possession of such deposited assets, however, to remain in the State Treasurer of Wisconsin pending the further order of the Court.

3. That the prosecution or the taking of any proceedings in and relative to the suit entitled "H. L. Currie vs. Fidelity Assurance Association" now pending in the Circuit Court for La Crosse County, Wisconsin, and the taking of any proceedings relative to any other suits which may have been commenced against said Association in the Courts of Wisconsin, and the commencement and prosecution of any and all actions against said Association in the Courts of the State of Wisconsin, is hereby enjoined.

4. That the expenses of the Banking Commission of Wisconsin in administering the business and assets of said Association located in Wisconsin be paid out of the assets of said Association located in the State of Wisconsin.

5. That the Banking Commission of Wisconsin be and the same hereby is authorized and empowered to forthwith ascertain the names and identity of all contract, bond or certificate holders and creditors of said Association located in Wisconsin, the nature of the contracts, bonds or certificates and claims held by each of such Wisconsin bond, contract or certificate holders and creditors and the respective amounts of such contracts, bonds or certificates and claims.

6. That the Banking Commission of Wisconsin be and the same is hereby empowered to seek from time to time the further advice of the Court and further orders relative to the administration of the assets of said Association.

7. That a copy of this order be forthwith served upon the said Fidelity Assurance Association, upon the State Treasurer of Wisconsin, upon the plaintiff's attorney in the aforementioned suit, entitled "H. L. Currie vs. Fidelity Assurance Association," now pending in the Circuit Court for La Crosse County, Wisconsin, upon any and all banks, depositaries or other persons, firms or corporations which the said Banking Commission of Wisconsin may find to have in possession any assets of said Association, and upon any and all persons whom said Banking Commission of Wisconsin may find to have commenced or to be about to commence any suit of any kind or nature against said Fidelity Assurance Association in the Courts of the State of Wisconsin.

8. Whenever a certified copy of this order shall be presented by the Banking Commission to any bank or

other depositary or debtor of said Association in the State of Wisconsin it shall constitute full authority for the payment or surrender to the Commission of any funds, property or assets of said Association demanded by said Commission.

9. It is further ordered that delivery of a copy of this order either before or after the commencement of any suit or other action herein enjoined shall constitute due notice to such person of the injunctions, prohibitions, restraints and orders herein contained and hereby ordered, as well as of all other terms and provisions hereof affecting any such person, and shall thereafter be binding upon such person, his agents, attorneys and representatives.

Dated April 14, 1941.

AUGUST C. HOPPMANN
Circuit Judge

SCHEDULE OF FIDELITY ASSURANCE ASSOCIATION BONDS SOLD BY BANKING COMMISSION OF WISCONSIN MAY 27, 1941 (From Ex. 120)

Issue	Rate	Maturity	Par	Price	SOLD FOR Principal Amount	Accrued Interest	Total Proceeds
Harriman—Ripley Company							
Remington-Rand, Inc.—20 Year Debenture (WW)	4¼%	3/1/56	$ 75,000.00	104-1/4	$ 78,187.50	$ 770.31	$ 78,957.81
Champion Paper & Fibre Co. S. F. Deb. (9/1/35)	4¾	9/1/50	11,000.00	106	11,660.00	126.27	11,786.27
Reading Company—General & Refunding B	4½	1/1/97	25,000.00	82	20,500.00	459.38	20,959.38
City of Ashland—Waterworks (12/1/35)	4	12/1/51	19,000.00	115.0498		373.67	
City of Ashland—Waterworks (12/1/35)	4	12/1/52	20,000.00	115.8567	74,475.24	393.33	75,733.91
City of Ashland—Waterworks (12/1/35)	4	12/1/54	22,000.00	117.7559		432.67	
City of Ashland—Waterworks (12/1/35)	4	12/1/56	3,000.00	117.9379		59.00	
U. S. Treasury Bonds	2¾	6/15/63-58	25,000.00	110-6/32	27,546.88	311.28	27,858.16
U. S. Treasury Bonds	2¾	12/15/65-60	150,000.00	110-19/32	165,890.63	1,867.71	167,758.34
U. S. Treasury Bonds	2¾	9/15/59-56	150,000.00	109-26/32	164,718.75	836.46	165,555.21
U. S. Treasury Notes	¾	9/15/44	617,000.00	100-7/32	618,349.69	930.53	619,280.22
TOTAL			$1,117,000.00		$1,161,328.69	$6,560.61	$1,167,889.30
First Boston Corporation							
Ohio Edison Company—1st Mtge.—Series 1935	4 %	11/1/65	$ 25,000.00	107-7/16	$ 26,859.38	$ 75.00	$ 26,934.38
U. S. Treasury Bond	3	9/15/55-51	1,000.00	112	1,120.00	6.08	1,126.08
TOTAL			$ 26,000.00		$ 27,979.38	$ 81.08	$ 28,060.46
Smith Barney & Company							
Wilson & Co.—Conv. Deb.	3¾%	4/1/47	$ 50,000.00	103-3/8	$ 51,687.50	$ 296.88	$ 51,984.38
Holley-Dayton & Gernon							
City of Kenosha—Street Widening (2/1/31)	4½%	2/1/45	$ 10,000.00	111.63	$ 11,163.65	$ 146.25	$ 11,309.90
GRAND TOTAL			$1,203,000.00		$1,252,159.22	$7,084.82	$1,259,244.04

AFFIDAVIT OF HOWARD L. SMITH, SPECIAL DEPUTY COMMISSIONER OF BANKING

(Exhibit 114)

(Caption Omitted)

Howard L. Smith being first duly sworn on oath deposes and says:

1. That he is an adult resident of the City of Madison, Dane County, Wisconsin, and is by profession a Certified Public Accountant, and that on the 25th day of April, 1941, he was duly appointed by the Banking Commission of Wisconsin, Special Deputy Commissioner of Banking to assist in the liquidation of the Wisconsin assets of the Fidelity Assurance Association, and that this appointment was confirmed by the Circuit Court for Dane County having jurisdiction of said proceedings.

2. That as such Special Deputy Commissioner of Banking, he has been since April 25th, 1941, in charge of the liquidation of the Wisconsin assets of Fidelity Assurance Association and has official custody and supervision over all of the records and files of said liquidation and has charge of all matters pertaining thereto.

3. That he prepared claim forms for the filing of claims of Wisconsin contract holders of Fidelity Assurance Association, and that he is familiar with the claims filed by said contract holders and with all of the correspondence had with such contract holders relating thereto.

4. That on said claim forms there was provided a space for "comments" to be made by said contract holders if they so desired, and that upon said claim forms which had been

filed in the approximate number of fifty-four hundred, many of said contract holders have voluntarily expressed their sentiments relative to possible reorganization of Fidelity Assurance Association and that of such contract holders so expressing themselves, a total of one hundred thirty-four have indicated clearly that they are in no way interested in a possible reorganization of Fidelity Assurance Association and are desirous of having paid to them the present value of their contracts.

5. That a number of said contract holders in the space provided for said "comments" have indicated that they purchased said contracts upon the express representations made by the salesman of Fidelity Assurance Association that the liability of the Association to them upon such contracts was fully protected by a deposit made with the State Treasurer of Wisconsin by said Association. A total of seventy-four of such contract holders have voluntarily expressed themselves in this manner.

6. That although in published notices given by the Banking Commission of Wisconsin it was indicated that a reorganization of said company might at some future time be effected, the overwhelming majority of those expressing themselves in this regard in the space provided for "comments" on the claim forms filed by them have as above stated, indicated that they desire to have the present value of their contracts paid to them.

7. That a number of Wisconsin contract holders have corresponded by letter with the Banking Commission of Wisconsin and have expressed themselves with respect to possible reorganization and also as to the representations upon which they purchased such contracts. In sixty-two letters containing expressions in this regard, contract hold-

ers have clearly indicated that they do not favor a reorganization of the company and desire to have paid to them the present value of their contracts, and in twenty-six of said letters which contained expressions in this regard, the contract holders stated that they had been assured by representatives of Fidelity Assurance Association that the liability of the company to them was fully protected by a deposit made with the State Treasurer of Wisconsin.

8. That of all the written communications received by way of "comments" attached to claim forms or by letters from contract holders aggregating over forty-three hundred in all, only eleven contract holders expressed themselves as in any way in favor of a possible reorganization of Fidelity Assurance Association, copies of these eleven communications being attached hereto and made a part hereof.

9. That affiant as such Special Deputy Commissioner of Banking has talked personally with a large number of contract holders aggregating to the best of his knowledge and belief between two and three hundred in number and that practically all of said contract holders expressed themselves as not being interested in possible reorganization plans affecting Fidelity Assurance Association and they desired to have the present value of their contracts paid to them by the Banking Commission of Wisconsin and that a great number of them further indicated that they had purchased their contracts on the express representation that the liability of the company to them was fully protected by a deposit made with the State Treasurer of Wisconsin by the company and that they were of the firm belief that the amount of this liability should not be reduced and that it should be paid to them.

10. That from his knowledge of the affairs of Fidelity Assurance Association in Wisconsin as such Special Deputy

Commissioner of Banking, affiant is firmly convinced that few, if any, Wisconsin contract holders would consent to a plan of reorganization which would involve a reduction in the present value of their contracts. That from his knowledge of said affairs, affiant is further convinced that said Wisconsin contract holders having purchased their contracts on the express representation that in the event of a default they would be protected by the Wisconsin deposits have become greatly aroused and incensed by reason of the fact that Fidelity Assurance Association has sought to prevent the prompt payment of their claims out of the Wisconsin deposits and have sought to have said deposits removed from the State of Wisconsin and subjected to the jurisdiction of a Federal Court in the Southern District of West Virginia. That by reason of the present attitude of Wisconsin contract holders affiant is of the belief that it would be extremely difficult, if not impossible, to secure the consent of any appreciable number of said contract holders to any proposed plan of reorganization involving any modification either of the present value or the matured value of their contracts.

Dated at Madison, Wisconsin, this 10th day of September, 1941.

Howard L. Smith
Special Deputy Commissioner
Banking Commission of Wisconsin

Subscribed and sworn to before me this
11th day of September, 1941.

Lucille Mueller
Notary Public, Dane County, Wisconsin
My Commission Expires: July 2, 1944

COMMENTS MADE TO BANKING COMMISSION OF WISCONSIN BY WISCONSIN CONTRACT HOLDERS IN CONNECTION WITH CLAIMS FILED, REFERRED TO IN PARAGRAPH 8 OF FOREGOING AFFIDAVIT AND ATTACHED THERETO

(Claim Forms to which Comments attached Omitted)

"Should you have any reorganization plan we would consider that rather than accept a cash settlement."—Obert Johnson, Osseo, Wis. (Claim No. 2253)

"As a matter of fact I am not anxious to cash in these contracts if the banking commission in West Virginia gets the company on its feet again. I received a letter in May from the commission asking if they should draw on my account as the Fidelity company had been doing and I gave them permission to do so. This money of course is in a separate fund but I presume the insurance these contracts represent is still in force. * * * The thought has just occurred to me that we in this state should at least receive the amount of money we actually paid in; instead of the cash surrender value as I have figured it; inasmuch as the banking department had at least 100% coverage on the money we sent out east."—W. B. Southard (Claim No. 2550)

"If Company is Reorganized intehd to leave amount in for ten years if possible and collect full amount at that time."—Ernest N. Peterson, Wausau, Wis. (Claim No. 1508)

"Don't intend to cash contract, as surrender value so small (for only a year). Hope this amount could be used for Insurance policy after firm is reorganized or leave amount in for 10 yrs. (14 months paid in $105.00)"—Hilda Zeier Peterson, Wausau, Wis. (Claim No. 1510)

"I have paid in $15.00 per mo. for eleven months—the cash surrender value is much less I know—I took a loss of $200.00 on a cash surrender of another contract—I think I

should have the $165 in this case. P.S. A reliable insurance policy (*reliable* company) will be acceptable—but not a loss of money paid in."—Frances K. Tipple, Taycheedah, Wis. (Claim No. 2245)

"If the Fidelity Association should prove solvent and reorganize then, I would want to resume my contract and not have to suffer the loss that this surrender makes. Will the warrant be honored under these circumstances? Before cashing takes place will a report be made to us on the status of Fidelity at the time? I do not want to take the cash surrender value if I can avoid that loss."—Ralph A. Borah. (Claim No. 2364)

"If a reorganization of the company is effected I would like to be notified of the details before final settlement of the cash surrender value is made."—Richard J. Feil, Madison, Wis. (Claim No. 2371)

"I don't know just what the cash surrender value of this contract would be but as of April 10 I have paid in 5 years and 2 months of $930 which does not take into account any interest they may have credited me with. If I understand their cash commuted value schedule this contract would rate the 6th coupon or $749 plus 2 extra months, which being 1/6 of the year would amount to $31. On these two contracts therefor I will be forced to take a loss of $300; less any interest I may have earned so as my inclosed letter states; I am not anxious to cash them in if the state of West Virginia can work out a plan that is feasible."—Willard B. Southard, Rice Lake, Wis. (Claim No. 2590)

"If reorganization takes place satisfied to continue with Company."—Joseph A. Rauch, Francis Creek, Wis. (Claim No. 2758)

"I should prefer to have my contract run to maturity rather than take the cash surrender value in the near future. Realizing the matter may be complicated, however,

I expect to accept the settlement agreed upon by others of this state. Nevertheless, I am continuing to make my payments to the trustees of the Company with the hope that a reorganization plan enabling payment of face of contracts may be achieved."—John K. Lanckton, Menomonie, Wis. (Claim No. 2764)

"If insurance setup to be proposed by Fidelity Assurance Association is satisfactory, I wish to take insurance instead of cash and surrender."—H. V. Foshion, Algoma, Wis. (Claim No. 4539)

AFFIDAVIT OF EMMETT G. HAMPTON

(Exhibit 114)

(Caption Omitted)

Emmett G. Hampton being first duly sworn on oath deposes and says:

1. That he is an adult resident of the City of Madison, Dane County, Wisconsin, and that he is regularly employed by the Banking Commission of Wisconsin as Supervisor of Credit Unions, and that at the request of the Banking Commission of Wisconsin, he assumed duties as Office Manager in connection with the liquidation of the Wisconsin assets of Fidelity Assurance Association, title to which Wisconsin assets became vested in the Banking Commission of Wisconsin on April 14, 1941, and which liquidation is now in process under the jurisdiction of the Circuit Court for Dane County, Wisconsin.

2. That as such Office Manager he had charge of all of the files and records in said liquidation proceedings affect-

ing Fidelity Assurance Association during the period from May 15, 1941, to August 1, 1941, during which period claims were being filed in said liquidation by Wisconsin contract holders of Fidelity Assurance Association.

3. That while acting as such Office Manager, he conducted correspondence with Wisconsin contract holders relative to claims in said liquidation and discussed with various contract holders, in person or by telephone, questions relating to the liquidation of the Wisconsin assets of Fidelity Assurance Association. Such personal interviews were had with contract holders aggregating to the best of his knowledge and belief between eight hundred and one thousand in number out of the total of approximately fifty-four hundred contract holders who have filed their claims with the Banking Commission of Wisconsin.

4. That a majority of said contract holders with whom he discussed these matters voluntarily expressed their entire satisfaction with the proceedings as conducted by the Banking Commission of Wisconsin and that it was their express desire that these proceedings should be continued and that in the event efforts should be made to have their claims adjusted in a Federal Court in bankruptcy or re-organization proceedings that it was their desire that the Banking Commission of Wisconsin make every effort to resist any such attempt to so adjust their rights and to continue the proceedings under the supervision of the Banking Commission and the Circuit Court for Dane County, Wisconsin; that these contract holders fully understood that the expenses of the liquidation conducted by the Banking Commission of Wisconsin would necessarily be paid out of the assets on deposit in Wisconsin for their benefit but that

they nevertheless were of the firm belief that the proceedings in Wisconsin should be continued.

5. That a great majority of said contract holders volunteered the information that they had purchased their contracts upon express assurance received from the salesman of Fidelity Assurance Association that the Association had on deposit with the State Treasurer of Wisconsin a sum equal to 110% of the Cash Value of Wisconsin contracts and that such sum was segregated apart from the other assets of the Association for the express benefit of Wisconsin contract holders; that a number of such contract holders further stated that prior to their purchase of the contracts they had checked the salesman's statements in this regard with the Banking Commission of Wisconsin and had ascertained that such was in fact the case; that a great majority of said contract holders further volunteered the information that they were not interested in any reorganization plan which would affect their rights against Fidelity Assurance Association but were now desirous of realizing the present value of their contracts as soon as possible; that of all of the contract holders with whom he discussed matters affecting their claims against Fidelity Assurance Association, only one suggested that he might be in favor of a reorganization of the company and then only if a reorganization would produce more than the present value of his contract.

6. That from his contact with said Wisconsin contract holders, affiant is convinced that any attempts to secure the continuance of payments by such contract holders to Fidelity Assurance Association upon a possible reorganization of said Association would fail, the overwhelming sentiment of such contract holders being that they desire to sever their relationship with Fidelity Assurance Association.

Dated at Madison, Wisconsin, this 10th. day of September, 1941.

Emmett G. Hampton
Supervisor of Credit Unions
State Banking Department

Subscribed and sworn to before me
this 11th day of Sept., 1941.

Lucille Mueller
Notary Public, Dane County, Wisconsin
My Commission Expires: July 2, 1944.

STATUTES OF IOWA, INSOFAR AS PERTINENT TO THE ISSUES IN THIS CASE, TO WHICH FIDELITY ASSURANCE ASSOCIATION WAS AND IS SUBJECT

Chapter 392

Sale of Stock on Installment Plan

8517 Terms defined. The term "association" when used in this chapter shall mean any person, firm, company, partnership, association, or corporation, other than building and loan associations and insurance companies and associations, which issue stocks on the partial payment or installment plan. The term "issue," shall mean issue, sell, place, engage in or otherwise dispose of or handle. The term "stock" shall mean certificates, memberships, shares, bonds, contracts, debentures, stocks, tontine contracts, or other investment securities or agreements of any kind or character issued upon the partial payment or installment plan.

8518 Certificate—how obtained. No association contemplated by this chapter shall issue any stock until it shall have procured from the commissioner of insurance a certificate of authority authorizing it to engage in such business. To procure such certificate of authority it shall be necessary for such association to file with the commissioner of insurance a statement, under oath, showing the name and location of such association, the name and post-office address of its officers, the date of organization, and if incorporated a copy of its articles of incorporation, also, a copy of its bylaws or rules by which it is to be governed, the form of its certificates, stocks, or contracts, all printed matter issued by it, together with a detailed statement of its financial condition and such other information concerning its affairs or plan of business as the commissioner of insurance may require.

8519 Approval by commissioner. If the commissioner of insurance is satisfied that the business is not in violation of law or of public policy, and is safe, reliable, and entitled to public confidence, and shall approve the form of certificate of stock or contract, he shall issue to such association a certificate of authority authorizing it to transact business within this state until the first day of March next succeeding the date of such authorization.

8520 Annual report. During the month of January of each year, every association transacting the business contemplated by this chapter, shall file with the commissioner of insurance a statement showing its condition on the thirty-first day of December preceding. Said statement shall be in such form as shall be prescribed by the commissioner of insurance. If it appears from such statement that such association is doing a safe business and is solvent, the commissioner of insurance may renew its certificate of authority authorizing it to transact business within the state until the first day of March of the following year. If at any time it shall appear that such association is doing an unsafe business or is insolvent the commissioner of insurance may revoke its certificate of authority authorizing it to transact business within the state until the first day of March of the following year. If at any time it shall appear that such association is doing an unsafe business or is insolvent the commissioner of insurance may revoke its certificate of authority to transact business and having revoked the certificate of authority of an association organized under the laws of this state, he shall report his action to the attorney general who shall at once apply to the district court or a judge thereof for the appointment of a receiver to close up the affairs of such association, and an injunction may issue in the same proceeding enjoining and restraining the association from transacting business in this state.

8521 Bonds or securities deposited. Before any association shall be authorized to transact business contemplated by this chapter, it shall deposit with the commissioner of insurance a bond approved by the commissioner of insurance, guaranteeing the faithful performance of all contracts entered into by such association or securities of the kind designated in subsections 1, 2, 3, 4, and 5 of section 8737, or such other securities as shall be approved by the commissioner of insurance in the amount of twenty-five thousand dollars, which amount shall remain in possession of the commissioner of insurance until the end of the calendar year in which the association shall first be authorized to transact business. At the end of such calendar year, such association shall deposit with the commissioner of insurance securities of the kind above provided in an amount equal to all its liabilities to persons residing within this state and shall keep such deposit at all times equal to such liability; provided that at no time shall such deposit be reduced below twenty-five thousand dollars except at such time as such association shall be by law closing out its business and its liabilities shall have been reduced below twenty-five thousand dollars.

8522 Unauthorized companies—penalty. Any member or representative of any association who shall attempt to issue or sell any stock as contemplated by this chapter or to transact any business whatsoever in the name of or on behalf of such association, not authorized to do business within this state, or which has failed or refused to comply with the provisions of this chapter, or has violated any of its provisions shall be deemed guilty of a misdemeanor and on conviction thereof shall be punished by imprisonment in the county jail not to exceed one year, or by a fine of not less than one hundred nor more than ten hundred dollars or by both such fine and imprisonment in the discretion of the court.

8524 Examination. Every such association doing business within this state, shall be subject to examination in the same manner as is provided for the examination of insurance companies and shall pay the same fees and costs therefor, and shall so far as is consistent with the plan of business, be subject to the same restrictions and regulations. Such examinations shall be full and complete and in making the same the commissioner of insurance or examiner shall have full access to and may demand the production of all books, securities, papers, moneys, etc., of the association under examination, and may administer oaths, summon and compel the attendance and testimony of any persons connected with such association. If upon such examination, it shall appear that such association does not conduct its business in accordance with law, or if it permits forfeiture of payments by persons holding its stock, after three years from the issuance of said stock or provides for the payment of its expenses other than from earnings, or that any profits, advantage, or compensation of any form or description is given to any member or investor over any other member or investor of the same class, or if beneficiaries are selected or determined or advantages given one over another by any form of chance, lottery, or hazard, or if certificates of stock are by their terms or by any other provision to be redeemed in numerical order or by any arbitrary order or precedence, without reference to the amount previously paid thereon by the holder thereof, or that the affairs are in an unsound condition, or if such association refuses such examination to be made, the commissioner of insurance may revoke its certificate of authority to do business in this state, and having revoked the certificate of authority of an association organized under the laws of this state, he shall report the same to the attorney general, who shall proceed as provided in section 8520.

Chapter 393.1

Iowa Securities Act

8581.02 Administration. The administration of the provisions of this chapter shall be vested in the commissioner of insurance of the state of Iowa.

The commissioner of insurance shall appoint a superintendent in charge of the securities department and may appoint one or more assistants. The superintendent appointed under this chapter shall perform such duties as the commissioner of insurance shall generally or specifically direct. In case of vacancy in the office of commissioner of insurance, by reason of absence, physical disability or other cause, to administer properly the provisions of this chapter, the superintendent appointed under this chapter shall act for and in the stead of the commissioner of insurance, and thereupon the superintendent shall have generally, for the time being, all the power and authority of this chapter conferred upon the commissioner of insurance.

8581.06 Registration of securities. No securities except of a class exempt under any of the provisions of section 8581.04 or unless sold in any transaction exempt under any of the provisions of section 8581.05 shall be sold within this state unless such securities shall have been registered by qualification as hereinafter defined. Registration of stock shall be deemed to include the registration of rights to subscribe to such stock if the application under section 8581.07 for registration of such stock includes a statement that such rights are to be issued.

* * *

8581.07 Registration by qualification. All securities required by this chapter to be registered before being sold in this state shall be registered only by qualification in the manner provided by this section.

The commissioner of insurance shall receive and act upon applications to have securities registered by qualification, and may prescribe forms on which he may require such applications to be submitted. Applications shall be in writing and shall be duly signed by the applicant and sworn to by any person having knowledge of the facts, and filed in the office of the commissioner of insurance and may be made either by the issuer of the securities for which registration is applied or by any registered dealer desiring to sell the same within this state.

The commissioner of insurance may require the applicant to submit to him the following information respecting the issuer and such other information as he may in his judgment deem necessary to enable him to ascertain whether such securities shall be registered pursuant to the provisions of this section:

* * *

The commissioner of insurance shall have power to place such conditions, limitations and restrictions on any registration as may be necessary to carry out the purposes of this chapter and the conditions, limitations and restrictions, if any, shall be entered in the register of securities or an entry shall be made in the register of securities referring to a formal order of the commissioner of insurance on file showing such conditions, limitations and restrictions.

* * *

If upon examination of any application the commissioner of insurance shall find that the sale of security referred to therein would not be fraudulent or would not work or tend to work a fraud upon the purchaser, or that the enterprise or business of the issuer is not based upon unsound business principles, he shall record the registration of such security in the register of securities, and thereupon such security so registered may be sold by the issuer or by any registered dealer, subject, however, to the further order of the commissioner of insurance as hereinafter provided.

So long as any security is sold or offered for sale pursuant to registration by qualification under this section, there shall be filed with the commissioner of insurance, each year, within ninety days after the termination of the fiscal year of the issuer of such security, a statement properly verified, which statement shall set forth the financial condition, the amount of assets and liabilities and such other information concerning the financial affairs or the plan of business of the issuer as the commissioner of insurance may require in order to determine whether the continued sale of such securities would result or tend to result in fraud; provided, however, that any applicant for registration by qualification may file with the commissioner of insurance a verified statement that applicant will make no further original distribution under the registration and one statement of condition as required by this paragraph either concurrently therewith or subsequent thereto and thereafter no statement shall be required under this paragraph.

* * * *

8581.08 May limit price and commission. The commissioner of insurance may also limit the price at which the securities, either of par or no par value, may be sold. In case of a sale by or on behalf of an issuer, the commissioner of insurance may allow a commission not to exceed twenty per cent of the sale price, such percentage to include all expenses incidental to such sale, including advertising or any other expense chargeable in any way to the sale of such securities.

8581.09 Consent to service. Upon any application for registration under this chapter where the issuer functions or intends to function as a dealer in the manner permitted by section 8581.11 and such issuer is not domiciled in this state, there shall be filed with such application the irrevocable written consent of the issuer that suits and actions, growing out of the violation of any provision or provisions

of this chapter, may be commenced against it in the proper court of any county in this state in which a cause of action may arise or in which the plaintiff may reside, by the service of any process or pleading authorized by the laws of this state, on the commissioner of insurance, said consent stipulating and agreeing that such service of such process or pleadings on such commissioner of insurance shall be taken and held in all courts to be as valid and binding as if due service had been made upon the issuer himself, and said written consent shall be authenticated by the seal of said issuer, if it has a seal, and by the acknowledged signature of any officer of the incorporated or unincorporated association, if it be an incorporated or unincorporated association, duly authorized by resolution of the board of directors, trustees or managers of the corporation or association, and shall in such case be accompanied by a duly certified copy of the resolution of the board of directors, trustees or managers of the corporation or association, authorizing the officers to execute the same. In case any process or pleadings mentioned in this chapter are served upon the commissioner of insurance, it shall be by duplicate copies, one of which shall be filed in the office of the commissioner of insurance and another immediately forwarded by registered mail to the principal office of the issuer against which said process or pleadings are directed.

8581.10 Revocation of registration of securities. The commissioner of insurance may refuse or revoke the registration of any security by entering an order to that effect, with his findings in respect thereto, if after a reasonable notice and a hearing or upon examination into the affairs of the issuer of such security it shall appear that the issuer:

1. Is insolvent; or

2. Has violated any of the provisions of this chapter or any order of the commissioner of insurance of which such issuer has notice; or

3. Has been or is engaged or is about to engage in fraudulent transactions; or

4. Is in any other way dishonest or has made any fraudulent representations in any prospectus or in any circular or other literature that has been distributed concerning the issuer or its securities; or

5. Is of bad business repute; or

6. Does not conduct its business in accordance with law; or

7. That its affairs are in an unsound condition, or

8. That the enterprise or business of the issuer is not based upon sound business principles.

In making such examination the commissioner of insurance shall have access to and may compel the production of all the books and papers of such issuer, and he or the superintendent may administer oaths to and examine the officers of such issuer or any other person connected therewith as to its business and affairs and may also require a balance sheet exhibiting the assets and liabilities of any such issuer or his income statement, or both, to be certified to by a public accountant either of this state or of any other state where the issuer's business is located, approved by the commissioner of insurance.

Whenever the commissioner of insurance may deem it necessary, he may also require such balance sheet or income statement, or both to be made more specific in such particulars as the commissioner of insurance shall point out or to be brought down to the latest practicable date.

If any issuer shall refuse to permit an examination to be made by the commissioner of insurance, it shall be proper ground for refusal or cancellation of registration.

If the commissioner of insurance shall deem it necessary he may enter an order suspending the right to sell securities pending any investigation or hearing, provided that the order shall state the grounds of the commissioner of insurance for taking such action.

Notice of the entry of such order shall be given personally or by telephone, telegraph, or mail to the issuer and every registered dealer who shall have notified the commissioner of insurance of an intention to sell such security.

8581.14 Revocation of dealers' and salesmen's registrations. Registration under section 8581.11 may be refused or any registration granted may be revoked by the commissioner of insurance if after a reasonable notice and a hearing the commissioner of insurance determines that such applicant or registrant so registered:

1. Has violated any provision of this chapter or any regulation made hereunder; or

2. Has made a material false statement in the application for registration; or

3. Has been guilty of a fraudulent act in connection with any sale of securities, or has been or is engaged or is about to engage in making fictitious or pretended sales or purchases of any of such securities or has been or is engaged or is about to engage in any practice or sale of securities which is fraudulent or in violation of the law; or

4. Has demonstrated his unworthiness to transact the business of dealer or salesman;

5. Has been convicted of a felony, or any misdemeanor of which an essential element is fraud;

6. Has made any representations or false statements to, or concealed any essential or material fact from, any person in the sale of a security to such person;

7. Has failed to account to persons interested for all money and/or property received;

8. Has not delivered after a reasonable time, to persons entitled thereto, securities held or agreed to be delivered by the dealer or broker, as and when paid, and due to be delivered;

9. Has made or is making misrepresentations of any essentials or material fact to the commissioner of insur-

ance, or has violated a provision of the laws of any foreign state regulating the sale of securities therein;

10. Is insolvent;

11. Is selling or offering for sale securities through any solicitor and agent not registered in compliance with the provisions of this chapter;

12. Has been refused a license in any state, or that any license in any state theretofore granted the applicant or registrant, or any officer, director, member or partner, manager or trustee thereof has been canceled, suspended or withdrawn for fraudulent conduct or violation of the law of such state regulating the sale of securities therein;

13. Is or has been using practices in the sale of securities that work or tend to work a fraud;

14. Has refused to furnish or give pertinent data to the commissioner of insurance;

* * *

It shall be sufficient cause for refusal or cancellation of registration in case of a partnership or corporation or any unincorporated association, if any member of a partnership or any officer or director of the corporation or association has been guilty of any act or omission which would be cause for refusing or revoking the registration of an individual dealer or salesman.

8581.15 Examinations and insolvency. The commissioner of insurance may compel every licensed dealer to make a report not later than the tenth of each month of all securities purchased and sold by such dealer and its salesmen during the preceding calendar month, and the books of all dealers, whether they are duly licensed or their license has been suspended, revoked or canceled, shall at all times be open to examination and inspection by the commissioner of insurance or any of his employees or any person delegated to examine them. If, upon examination, it is found that the dealer is insolvent or if the records are in such condi-

tion that the examiner is unable to determine the financial condition of the dealer, the commissioner of insurance may ask the appointment of a receiver to safeguard the interests of the public; the district court in Polk county or the county in which such dealer has its principal place of business shall have authority to appoint such receiver.

8581.21 Injunctions. Whenever it shall appear to the commissioner of insurance, either upon complaint or otherwise, that in the issuance, sale, promotion, negotiation, advertisement, or distribution of any securities within this state, including any security exempted under the provisions of section 8581.04, and including and transaction exempted under the provisions of section 8581.05, any person, as defined in this chapter, shall have employed or employs, or is about to employ any device, scheme or artifice to defraud or for obtaining money or property by means of any false pretense, representation or promise, or that any such person shall have made, makes or attempts to make, in this state fictitious or pretended purchases or sales of securities or shall have engaged in, or engages in or is about to engage in any practices or transaction or course of business relating to the purchase or sale of securities which is in violation of law or which is fraudulent or which has operated or which would operate as a fraud upon the purchaser, any one or all of which devices, schemes, artifices, fictitious or pretended purchases or sales of securities, practices, transactions and courses of business are hereby declared to be and are hereinafter referred to as fraudulent practices; or that any person acting as a dealer or salesman within this state without being duly registered as such dealer or salesman as provided in this chapter, the commissioner of insurance may:

• • •

2. Examine the promoter, seller, broker, dealer, negotiator, advertiser or issuer of any such securities, and any agents, employees, partners, officers, directors, mem-

bers or stockholders thereof, under oath; and examine such records, books, documents, accounts and papers as may be relevant or material to the inquiry. For this purpose the commissioner of insurance shall have power to require by subpoena the attendance and testimony of witnesses and the production of papers, and the commissioner of insurance may sign subpoenas, administer oaths, and affirmations, examine witnesses and receive evidence. The fees and mileage shall be the same as prescribed by law in judicial procedure in the courts of this state in civil cases. Any party to any hearing before the commissioner of insurance, shall have the right to the attendance of witnesses in his behalf at such hearing, upon making a request therefor to the commissioner of insurance and designating the person or persons sought to be subpoenaed.

* * *

5. Whenever it shall appear to the commissioner of insurance from any report or statement filed, from any examination made as provided for in this chapter, or from any other source that any person, as defined in this chapter, has engaged in, is engaged in or is about to engage in any practice declared to be illegal and prohibited by the chapter, or that it will be against public interest for any person, as defined in this chapter, to issue, sell, offer for sale, purchase, offer to purchase, promote, negotiate, advertise or distribute any securities within or from this state, he may by petition apply to a court of equity for a writ of injunction or the appointment of a receiver, or both. The said petition shall allege that it appears to the commissioner of insurance from an investigation made in accordance with the provisions of this chapter, that such person, as defined in the chapter, is engaged in or is about to engage in practices declared to be illegal and prohibited or that it is against public interests for such person, as defined in this chapter, to issue, sell, offer for sale, purchase, offer to purchase, promote, negotiate, advertise or distribute any securities within

or from this state, which allegations may be verified generally, and on the filing of said petition the court may issue an injunction restraining such person from continuing such practices or engaging therein or doing any acts in furtherance thereof and/or the court may issue an injunction restraining the issuance, sale, offer for sale, purchase or offer to purchase, promotion, negotiation, advertisement, or distribution within or from this state, of any securities by such person and any agents, employees, brokers, partners, officers, directors or stockholders thereof, until the court shall otherwise order.

(Other portions of Chapter 393.1 omitted as not pertinent.)

Chapter 386

Permits To Foreign Corporations

8420. Application for permit. Any corporation for pecuniary profit organized under the laws of another state, or of any territory of the United States, or of any foreign country, which has transacted business in the state of Iowa since September 1, 1886, or desires hereafter to transact business in this state, and which has not a permit to do such business, shall file with the secretary of state a certified copy of its articles of incorporation, duly attested by the secretary of state or other state officer in whose office the original articles were filed, accompanied by a resolution of its board of directors or stockholders authorizing the filing thereof, and also authorizing the service of process to be made upon any of its officers or agents in this state engaged in transacting its business, and requesting the issuance to such corporation of a permit to transact business in this state: said application to contain a stipulation that such permit shall be subject to the provisions of this chapter.

8421. Details of application—secretary of state as process agent. Said application shall also contain a statement subscribed and sworn to by at least two of the principal officers of the corporation, setting forth the following facts, to-wit:

1. The total authorized capital of the corporation.
2. The total paid up capital of the corporation.
3. The total value of all assets of the corporation, including money and property other than money represented by capital, surplus, undivided profits, bonds, promissory notes, certificates of indebtedness or other designation, whether carried as money on hand or in bank, real estate or personal property of any description.
4. The total value of money and all other property the corporation has in use or held as investment in the state, at the time the statement is made (if any).
5. The total value of money and all other property the corporation proposes or expects to make use of in the state, during the ensuing year.
6. Certified copy of the resolution of the board of directors of said corporation giving name and address in Iowa of a resident agent on whom the service of original notice of civil suit in the courts of this state may be served. Failing which, or in the event such agent may not be found within the state, service of such process may then be made upon said corporation through the secretary of state by sending the original and two copies thereof to him, and on the original of which he shall accept service on behalf of said corporation, retain one copy for his files and send the other by registered mail to the corporation at the address of its home office as shown by the records in his office, which service shall have the same force and effect as if lawfully made upon said corporation within the county where such civil suit could be maintained against it under the laws of this state.

§422. **Secretary of state to determine values.** The secretary of state can make such independent and further investigation as to the property within this state owned by any such corporation as he may desire, and upon the true facts determine the value thereof, and fix the fee to be paid by such company.

(Other portions of Chapter 386 omitted as not pertinent.)

DECREE AND ORDER OF DISTRICT COURT, POLK COUNTY, IOWA, APPOINTING PERMANENT RECEIVER

(Part of Ex. 121)

(Caption Omitted)

Now on this 19th day of May, A. D., 1941, the same being one of the regular days of the May 1941 term of said Court, this matter comes on for final hearing before the Honorable John J. Halloran, one of the Judges of the above named Court, upon the application and petition of G. R. Shaw for the appointment of a receiver for the above named Company, the answer and cross-petition of the defendant and intervenor Chas. R. Fischer, Commissioner of Insurance of the State of Iowa, for the appointment of a permanent receiver, the petition of the State of Iowa through its Attorney General John M. Rankin for the appointment of a permanent receiver, and the petition of intervention of E. G. Pullen for the appointment of a permanent receiver. Plaintiff's proof of service of notice upon the defendant corporation and upon H. Isaiah Smith, one of the receivers appointed by the Circuit Court, Kanawha County, State of West Virginia, for the defendant

corporation, are thereupon submitted, and the Court finds that on the 24th day of April, A. D., 1941, this Court entered an order appointing Chas. R. Fischer, Commissioner of Insurance of the State of Iowa, receiver pendente lite, and fixing the 10th day of May, A. D., 1941, at 9:00 o'clock, A. M., at the Court House in Des Moines, Polk County, Iowa, before the Honorable John J. Halloran, as the date, time, and place of hearing upon the application and petition for the appointment of a permanent receiver for said defendant corporation and its assets within the State of Iowa, and to show cause why its affairs and business in the State of Iowa should not be wound up and its assets distributed to Iowa creditors as by law provided, and that said order further provided that notice of the date, time, and place of hearing upon the application and petition for the appointment of a permanent receiver should be given by personal service upon the defendant corporation and upon the parties named in said order, and that notice was given to the defendant corporation and upon H. Isaiah Smith, one of the receivers appointed by the Circuit Court of Kanawha County, State of West Virginia, the state of the said defendant corporation's domicile, as provided for in said order.

The plaintiff, G. R. Shaw, and the intervenor, E. G. Pullen, appear now by their attorneys Carl J. Stephens and Ben C. Buckingham, the intervenor, State of Iowa by its Attorney General John M. Rankin and Asst. Attorney General Floyd Philbrick, and that the defendant-cross-petitioner Chas. R. Fischer, Commissioner of Insurance of the State of Iowa, appears by Attorney General John M. Rankin and Asst. Attorney General Floyd Philbrick, and that the

defendant, Fidelity Assurance Association, appears not and its default is hereby entered against it.

And the Court having examined the files in said cause, the notices and the return of service thereon, and having examined the evidence submitted, heard the statements of counsel, and being fully advised in the premises, FINDS:

That the defendant corporation is a corporation organized and existing under and by virtue of the laws of the State of West Virginia, engaged in the business, among other things, of offering for sale and selling installment and annuity investment contracts;

That on or about the 11th day of April, 1941, upon complaint of E. G. Sims, Auditor of State of the State of West Virginia, and ex-officio Insurance Commissioner of said state, an order was entered by the Circuit Court of Kanawha County, State of West Virginia, finding that said defendant corporation was insolvent and was unable to meet its matured and maturing obligations and to pay its creditors, and that the further continuance of its business would be hazardous to the best interests of its contract holders, creditors, and the public, and that it was necessary for the preservation of the property and assets of said defendant corporation and of the respective rights of its creditors and stockholders that the same should be administered through a receiver or receivers, and ordering and decreeing the appointment of H. Isaiah Smith and Ross B. Thomas Receivers of said defendant corporation and of its property and assets, and that the said H. Isaiah Smith and Ross B. Thomas are the duly appointed, qualified, and acting receivers in the State of West Virginia of said defendant corporation;

That the defendant corporation was, upon its application and order of the Executive Council of the State of Iowa entered on the 7th day of January, 1929, issued a certificate of authority by the Auditor of State of the State of Iowa pursuant to the provisions of Chapter 392, Code of Iowa, 1927, authorizing it to engage in the business in the State of Iowa of offering for sale and selling installment and annuity investment contracts to persons residing within the State of Iowa;

That pursuant to the provisions of said Chapter 392, the defendant corporation, as a condition precedent to the issuance of certificate of authority and its engaging in business in the State of Iowa, deposited with the Auditor of State of the State of Iowa securities in the amount of Twenty-five Thousand ($25,000) Dollars, guaranteeing the faithful performance of contracts sold by it to persons residing in Iowa, and that since said original deposit it has supplemented the same and maintained said deposit in an amount equal to all of its liability to Iowa contract-purchasers and now has on deposit with the Commissioner of Insurance of the State of Iowa, pursuant to the provisions of Chapter 392, Code of Iowa, 1927, as amended by the Acts of the 48th General Assembly, securities of the par value of Forty-two Thousand ($42,000) Dollars;

That said defendant corporation, according to the evidence submitted, has a present liability to Iowa contract purchasers approximating somewhere between Thirty-five Thousand ($35,000) Dollars and Forty-five Thousand ($45,000) Dollars;

That the defendant corporation filed application with the Secretary of State, State of Iowa, on or about the 17th

day of December, 1937, for qualification as a foreign corporation under and pursuant to the provisions of Chapter 386, Code of Iowa, 1931, and that permit was issued by the Secretary of State to said corporation;

That with its said application it filed resolution of its board of directors designating Walter L. Keck, Maquoketa, Iowa, as its resident agent, and consenting to the service of process on him pursuant to the provisions of said Chapter 386, and that the said Walter L. Keck is now the resident agent of said defendant corporation;

That the defendant corporation did on or about the 28th day of March, 1930, file its application with the Secretary of State of the State of Iowa, for registration of securities as an issuer-dealer of securities pursuant to and in compliance with the provisions of the Iowa Securities Law as contained in Chapter 393, Code of Iowa, 1927, and that pursuant to said application said defendant corporation was authorized to sell in Iowa installment and annuity investment contracts, and that pursuant to said registration and said Chapter 393, Code of Iowa, 1927, said defendant corporation did file with the Secretary of State, State of Iowa, its written consent without power of revocation that suits and actions might be commenced against it in the State of Iowa by the service of process upon the Secretary of State of the State of Iowa;

That said defendant corporation's registration was cancelled sometime during the year 1936 in accordance with the laws of the State of Iowa;

That the said defendant corporation did sell its installment annuity investment contracts to persons residing in Iowa, and that the plaintiff, G. R. Shaw, and the intervenor,

E. G. Pullen, are contract holders as alleged in the plaintiff's petition and the said intervenor's petition, and that each, as well as other Iowa contract purchasers, has an interest in the assets of the defendant corporation now on deposit with the defendant-cross-petitioner Chas. R. Fischer, Commissioner of Insurance of the State of Iowa, and that said deposit constitutes a trust fund for the benefit of said plaintiff, intervenor and other Iowa contract purchasers;

That Chas. R. Fischer, Commissioner of Insurance of the State of Iowa, was, pursuant to the order of this Court entered on the 24th day of April, A. D., 1941, appointed receiver pendente lite of the defendant corporation and its assets located and situated within the State of Iowa, and that the said Chas. R. Fischer qualified as such receiver by filing surety bond approved by the Clerk of this Court and by taking his oath on the 24th day of April, 1941, and now has in his possession as such the securities deposited by said defendant corporation with him as Commissioner of Insurance of the State of Iowa, pursuant to the provisions of Chapter 392, Code of Iowa, 1939;

That the defendant corporation is insolvent, and that the further continuance of its business in the State of Iowa would be hazardous to its contract purchasers, creditors, and the public, and that a permanent receiver should be appointed for said defendant corporation in the State of Iowa as prayed to take charge and possession of its assets situated within the State of Iowa for the purpose of winding up the affairs and business of said defendant corporation, and for the purpose of distributing the same to the Iowa contract purchasers for whose benefit said assets were deposited in accordance with the provisions of Chapter 392,

Code of Iowa, 1939, and such other creditors as may by the laws of this state be entitled to the same;

That this Court has jurisdiction to appoint a permanent receiver for the defendant corporation, and its assets located in the State of Iowa, and to grant the relief prayed for by the parties to this cause of action.

NOW, THEREFORE, IT IS FINALLY ORDERED, ADJUDGED AND DECREED:

That under and pursuant to the statutes and laws of this state that the business and affairs of the defendant, Fidelity Assurance Association, in the State of Iowa be dissolved, closed up, and its assets situated within the State of Iowa administered and distributed in accordance with the laws of this state to Iowa contract purchasers of the defendant corporation, and such others as may be entitled to the same;

That Chas. R. Fischer, Commissioner of Insurance of the State of Iowa, be, and he is hereby appointed permanent receiver of said defendant corporation in accordance with the statutes and laws of this state with authority and direction to take charge of and manage the property, assets, and business of the defendant corporation within the State of Iowa with full power to sue for, collect, receive, and take into his possession the goods, chattels, rights, credits, moneys, books, papers, property and assets of every description and wherever stiuated in the State of Iowa of the defendant corporation, and to do any and all acts and things which may be necessary, proper, or advisable to preserve the property, assets, rights and privileges of the defendant corporation, and with all the incidental powers ordinarily vested in receivers in like cases;

That said receiver shall, as soon as it may be practicable, file an inventory of all property of every description that shall have come into his possession as such receiver;

That said receiver be, and he is, hereby directed to proceed to wind up the business of the defendant corporation in the State of Iowa and to that end all installment annuity investment contract purchasers and creditors, including all lien and unsecured creditors of the defendant and all claimants to specific assets in the hands of the receiver, be, and they hereby are ordered to file proof of their claim with the Clerk of the District Court on or before the 20th day of August, A. D., 1941;

That every proof of claim shall be itemized and sworn to and shall state the particularity, nature, and origin of the claim so asserted, the actual consideration therefor, when the same has become or will become due, whether any or what securities are held, whether any or what payments have been made thereon, and the sum claimed is justly due, and that the claimant has not, nor has any other persons for his use, received any security or satisfaction whatever, other than by him set forth;

That said receiver shall, within thirty (30) days from the date hereof, give notice to creditors of the defendant corporation advising them with respect to filing of claim, the powers of receiver with respect thereto, as herein set forth, and the time within which all claims shall be filed, by publishing the same in at least three newspapers of general circulation in the State of Iowa once each week for two consecutive weeks, the first publication thereof to be not later than the 3rd day of June, A. D., 1941;

That said receiver is authorized to examine the claims so filed, as heretofore provided, and to make his findings

thereon allowing or disallowing, in whole or in part, each and all of said claims, and to file in this cause as soon as possible after the time for filing claims has expired written report setting forth for the confirmation of this Court the results of such findings, subject to the right of any claimant to object to any findings so made, such objection to be filed in writing in this cause at such time as the Court may hereafter prescribe;

That in the event that any creditor, creditors, or claimants shall not so present or file their claims with the receiver aforesaid on or before the 20th day of August, A. D., 1941, it is hereby ordered that they shall be debarred from participating in any dividend or distribution that may hereafter be made in these proceedings, or from any interest in and to the assets of the defendant corporation administered by the receiver or any proceeds derived from the sale or other distribution thereof;

That the receiver be, and he is, hereby directed to cause all of the assets of the defendant corporation located within the State of Iowa, and coming into his hands as said receiver, to be appraised by two (2) competent appraisers whom the receiver shall select, and who shall report to this Court before any sale is made of the same and findings with respect to the value of the assets so appraised;

That the receiver be, and he is, further authorized and directed to sell all of the assets of the defendant corporation situated within the State of Iowa, and coming into his hands as said receiver, at either private or public sale, free and clear of all liens and encumbrances, but subject, however to the expenses of the receivership and the costs;

That the receiver be, and he is, hereby authorized to

employ Carl J. Stephens and his associate, Ben C. Buckingham, as counsel to advise him in the performance of his duties as receiver, and that he shall have leave to employ such agents or employees as may be necessary to enable him to properly perform his duties as said receiver;

That the said Chas. R. Fischer before entering upon his duties herein shall take an oath and file a bond with the Clerk of this Court as receiver, which bond shall be in the sum of $10,000.00, with sureties to be approved by the Clerk of this Court, conditioned that said receiver shall well and truly perform the duties of his office; whereupon letters of receivership shall issue to him;

That the said Chas. R. Fischer shall file his report as receiver pendente lite with this Clerk, and upon approval thereof he shall stand discharged as receiver pendente lite;

That the title to the assets deposited by the defendant corporation pursuant to the provisions of Chapter 392, Code of Iowa, 1927, vested at the time and times said securities were deposited and were at the time of the appointment of the receivers for the defendant corporation by the Circuit Court of Kanawha County, State of West Virginia, and at the time of the appointment by this Court of Chas. R. Fischer, as receiver pendente lite of the defendant corporation, held by the said Chas. R. Fischer, Commissioner of Insurance of the State of Iowa, in trust for the benefit of contract purchasers of said defendant corporation residing in Iowa, and that the title to said deposited securities be, and the same is, hereby vested in the said Chas. R. Fischer as permanent receiver of said defendant corporation for the benefit of the contract purchasers for whom the same were deposited to be distributed in accordance with

this order and decree and the subsequent orders of this Court;

That the findings of this Court, as herein contained, be, and the same are, hereby made a part of the order and decretal portion of this order and decree with the same force and effect as if specifically set out therein;

That this Court retains jurisdiction of this cause for the purpose of giving such further directions and the granting and entering of such orders, supplemental orders or decrees as may be necessary and proper in connection with the winding up of the affairs and business of the defendant corporation within the State of Iowa, and the administration and distribution of the assets of said defendant corporation situated within the State of Iowa, and coming into the hands of the receiver.

John J. Halloran

JUDGE, NINTH JUDICIAL DISTRICT OF IOWA

STATES, INCLUDING TERRITORIES OF ARIZONA AND NEW MEXICO, WHICH IN 1910 OR PRIOR THERETO CLASSIFIED LIFE INSURANCE COMPANIES AS SUCH BY REASON OF THE WRITING OF LIFE INSURANCE POLICIES AND THE PURCHASE AND SALE OF ANNUITIES

Territory of Arizona

"797. (Sec. 37.) Every corporation formed under the laws of this territory for the purpose of mutual insurance on the lives or health of persons, or against accidents to persons for life or any fixed period of time, or to purchase and sell annuities, must have a capital stock of not less than one hundred thousand dollars. * * *."

Revised Statutes of Arizona (1901) Title 13, Ch. 3, Insurance Corporations, sec. 797.

California

"594. Insurance classified. All insurance business in the State of California is hereby classified in the following sixteen kinds, namely:

"[Life insurance.] 1. Life insurance, including within its meaning insurance upon the lives of persons and every insurance appertaining thereto, and the granting, purchasing and disposing of annuities.

"* * *"

(The section was first enacted in substantially the form set out by Stats. and Amdts. 1907, 141.)

Kerr's Cumulative Supplement (1906-1913) California Political Code.

Colorado

"3116. Purposes of organization.

"Sec. 30. It shall be lawful for any insurance company organized under the laws of this state:

"* * *

"Second: To make insurance upon the lives of persons and every insurance appertaining thereto or connected therewith, including health and accident insurance, and to grant, purchase or dispose of annuities."

Courtright's Colorado Statutes (1908) p. 1140. (Laws 1907, p. 451.)

Connecticut

Sec. 3540 "Annuities may be issued by companies. Insurance companies chartered by and doing business in this state, and empowered to make contracts contingent upon life, may grant and issue annuities either in connection with or separate from contracts of insurance predicated upon life risks; and all such annuities heretofore issued by such companies shall be valid."

General Statutes of Connecticut (1902).

Illinois

"177. Number of persons who may organize, etc.] Sec. 1a. Any number of persons, not less than nine, may organize an incorporated company to make insurance upon the lives of persons, and every insurance pertaining thereto, or connected therewith, and to grant or dispose of annuities."

Revised Statutes of Illinois, Hurd (1909) Ch. 73, Insurance, sec. 177.

Indiana

"4678. Life Insurance—Stock or mutual plan.—1. That any ten or more persons, citizens of this state, may associate in accordance with the provisions of this act, and form an incorporated company for the following purposes: To make insurance, either upon the stock or mutual prin-

ciple, upon the lives of individuals, and every insurance appertaining thereto or connected therewith, and to grant and purchase annuities."

Burns' Annotated Indiana Statutes, Revision of 1908, Vol. 2, sec. 4678.

Kansas

"4111. Charter of life insurance company; by-laws, etc. Sec. 43. Every company or coporation formed or organized pursuant to chapter 23 of the General Statutes of 1868 for the purpose of making insurance on the lives of individuals shall file in the office of superintendent of insurance a copy of its charter, duly certified by the secretary of state, and it shall also file a copy of its by-laws, which shall set forth the number of its directors or trustees, which shall not be less than five nor more than twenty-five, and the manner of electing the same, and their term of office respectively, a majority of whom shall be citizens of this state, the times of holding elections, and the manner of filling vacancies. And every such company shall thereafter have power to make insurance on lives of individuals, and every assurance pertaining thereto or connected therewith, and to grant, purchase and dispose of annuities and endowments of every kind and description whatever. [L. 1871, ch. 93, sec. 44; March 24.]"

General Statutes of Kansas, Dassler, (1909), sec. 4111.

Kentucky

"4366. Any number of persons, not less than thirteen, may associate and form a corporation to (make) insurance upon the lives of individuals, and every insurance appertaining thereto, or connected therewith, and to grant, purchase or dispose of annuities and endowments of any kind." (Act April 5, 1893.)

Statutes of Kentucky, Russell (1909) Life Insurance and Life Insurance Companies, Art. 7, sec. 4366.

Louisiana

"3563. [Sec. 1, Act 203, 1908, p. 301.] It shall be lawful for any number of persons, not less than fifteen, citizens of the United States, and residents of this State on compliance with the provisions following, to form insurance companies on the stock plan, for any of the following purposes, to wit:

"* * *

"Third. To insure the lives or the health of persons, and every insurance appertaining thereto, and to grant, purchase or dispose of annuities."

Marr's Annotated Revised Statutes of Louisiana, Vol. 2, p. 1217.

Maryland

"148. Every corporation formed under the provisions of this article for the purposes of life insurance is hereby authorized also to insure individuals against accident, and to grant, purchase or dispose of annuities, unless it be otherwise provided in its charter or by-laws."

Public General Laws of Maryland, (1904) Vol. I, Art. 23, sec. 148.

Massachusetts

"Section 118. All companies doing business in the commonwealth under any charter, compact, agreement or statute of this or any other state, involving the payment of money or other thing of value to families or representatives of policy and certificate holders or members, conditioned upon the continuance or cessation of human life, or involving an insurance, guaranty, contract or pledge for the payment of endowments or annuities, shall be deemed to be life companies, and shall not make any such insurance, guaranty, contract or pledge in the commonwealth, or to or with any resident thereof, which does not distinctly state

the amount of benefits payable, the manner of payment and the consideration therefor, nor any such insurance, guaranty contract or pledge the performance of which is contingent upon the payment of assessments made upon survivors. * * *." (Acts & Resolves of Massachusetts 1907, ch. 576, sec. 66,)

General Laws of Massachusetts (1921) Vol. 2, Ch. 175, sec. 118.

Michigan

"(9323) Section 1. Thirteen or more persons may become a corporation for the purpose of making any of the following kinds of insurance:

First, Upon the lives and health of persons and every insurance pertaining thereto, and to grant, purchase or dispose of annuities; * * *." (Act 77, 1869, p. 124.)

Compiled Laws of Michigan, (1915) Vol. 2, p. 3375.

Minnesota

"1687 Defined—Every corporation or association, domestic or foreign, operating upon any plan involving payment of money or other thing of value to policy or certificate holders, or members, or families, or representatives of either, conditioned upon the continuance or cessation of human life, or for the payment of endowments or annuities (except benevolent, fraternal, cooperative, or secret societies or orders for the sole purpose of mutual welfare, protection, and relief of their members, and the payment of stipulated amounts, or the proceeds of assessments, to the families of deceased members), shall be deemed a life insurance company, and shall make no such insurance, guaranty, contract, or pledge in this state, or to or with any citizen or resident thereof, which does not distinctly specify the amount and manner of payment of benefits and the consideration therefor. ('95 c. 175 s. 63; '01 c. 143)"

Revised Laws of Minnesota (1905) sec. 1687.

Mississippi

"2598 (2339) Life insurance companies defined.—All corporations, associations, partnerships or individuals doing business in this state under any charter, contract, agreement or statute, of this or any other state, involving the payment of money or other things of value to families or representatives of policy and certificate holders or members, conditioned upon the continuance or cessation of human life, or involving an insurance, guaranty, contract or pledge for the payment of endowments or annuities, or who shall employ agents to solicit such business, shall be deemed to be life insurance companies and shall in all respects be subject to the laws herein made and provided for the government of life insurance companies, and shall not make any such insurance, guaranty, contract or pledge in this state with any citizen or resident thereof which does not distinctly state the amount of benefits payable, the manner of payment and the consideration therefor."

Mississippi Code (1906) sec. 2598.

Missouri

"Sec. 6895. Purposes for which formed.—Any number of persons, not less than thirteen, may associate and form a company for the purpose of making assurance upon the lives of individuals, and every assurance pertaining thereto or connected therewith, and to grant, purchase and dispose of annuities and endowments of every kind and description whatsoever, and to provide an indemnity against death; and for weekly or other periodic indemnity for disability occasioned by accident to the person of the insured; but such accident insurance shall be made a separate department of the business of the life insurance company undertaking it."

Revised Statutes of Missouri (1909) Vol. 2, sec. 6895.

Montana

"4016. *Definitions and classifications.*—Corporations, Associations, and Societies organized to do the following described business are insurance corporations within the meaning of this Act.

"* * *

"Second: To insure the lives and health of persons and to grant, purchase or dispose of annuities."

Revised Codes of Montana (1907) sec. 4016.

New Jersey

"1. Insurance companies; incorporation; purposes.—Ten or more persons may become a corporation for the purpose of making any of the following kinds of insurance, to wit:

"* * *

"—Life.—III. Upon the lives or health of persons, and every insurance appertaining thereto, and to grant, purchase or dispose of annuities;" (Ch. 134, Laws of New Jersey 1902).

Compiled Statutes of New Jersey (1709-1910) Vol. 2, p. 2838.

Territory of New Mexico

"Sec. 2846. Insurance Companies—General powers.

"Sec. 46 It shall be lawful for any insurance company to transact business in this State;

"* * *

"Second—To make insurance upon the lives of persons and every insurance appertaining thereto or connected therewith, including health and accident insurance, and to grant, purchase or dispose of annuities.

"* * *

"Act of Mar. 17, '09; L. '09, C. 48, sec. 25."

New Mexico Statutes Annotated (1915) sec. 2846.

New York

"Sec. 70. Incorporation. Thirteen or more persons may become a corporation for the purpose of making any of the following kinds of insurance:

"1. Upon the lives or the health of persons and every insurance appertaining thereto, and to grant, purchase or dispose of annuities."

Consolidated Laws of New York (1909) Vol. III, Article 2, sec. 70.

North Carolina

"4773. Life insurance company defined; requisites to contracts. All corporations, associations, partnerships or individuals doing business in this state, under any charter, compact, agreement or statute of this or any other state, involving the payment of money or other thing of value to families or representatives of policy and certificate holders or members, conditioned upon the continuance or cessation of human life, or involving an insurance, guaranty, contract or pledge for the payment of endowments or annuities, or who shall employ agents to solicit business, shall be deemed to be life insurance companies, shall in all respects be subject to the laws herein made and provided for the government of life insurance companies, and shall not make any such insurance, guaranty, contract or pledge in this state with any citizen, or resident thereof, which does not distinctly state the amount of benefits payable, the manner of payment and the consideration therefor."

Revisal of 1905 of North Carolina, Vol. 2, sec. 4773.

Ohio

"Sec. 3587. Any number of persons, not less than thirteen, may associate and form a company to make insurance upon the lives of individuals, and every insurance apper-

taining thereto or connected therewith, on the mutual or stock plan, and grant, purchase, or dispose of annuities."

Revised Statutes of Ohio (1890) Vol. 1, Ch. 10, sec. 3587.

Oklahoma

"3404. Incorporation of companies authorized—kinds of insurance classified. Ten or more persons may form a corporation for the purpose of making any of the following kinds of insurance, to-wit:

"* * *

"Third. Upon the lives or health of persons, and every insurance appertaining thereto, and to grant, purchase or dispose of annuities."

Revised Laws of Oklahoma (1910) Vol. I, sec. 3404.

Oregon

"Sec. 4629. Life Insurance Companies Defined.

"All corporations, associations, partnerships, or individuals doing business in this state under any charter, compact, agreement, or statute of this or any other state, involving the payment of money or other things of value to families or representatives of policy or certificate holders or members conditioned upon the continuance or cessation of human life, or involving an insurance, guaranty, contract, or pledge for the payment of endowments or annuities shall be deemed to be life insurance companies, and shall not make any such insurance, guaranty, contract, or pledge in this state or to or with any citizen or resident thereof, which does not distinctly state the amount of benefits payable, the manner of payment and the consideration therefor, nor any such insurance, guaranty, contract, or pledge the performance of which is contingent upon the payment of assessments made upon survivors; *provided, however*, the provisions of this section shall not relate to or interfere with the provisions of section 4658 and 4659 of this Code. [L. 1907, c. 216, p. 376.]"

Lord's Oregon Laws (1910) Vol. 2, sec. 4629.

Pennsylvania

"Insurance

"I. Incorporation of insurance companies.

"1. Any ten or more persons, citizens of this Commonwealth, may associate in accordance with the provisions of this act and form an incorporated company for any of the following purposes, to wit:

"* * *

"3. Second. To make insurance either upon the stock or mutual principle, upon the lives of individuals and every insurance appertaining thereto or connected therewith, and to grant and purchase annuities."

Brightly's Digest of Laws of Pennsylvania (1893-1903) p. 342.

Texas

"Article 4724. Terms defined.—A life insurance company shall be deemed to be a corporation doing business under any charter involving the payment of money or other thing of value, conditioned on the continuance or cessation of human life, or involving an insurance, guaranty, contract or pledge for the payment of endowments or annuities. * * * [Acts 1909, p. 192, sec. 1.]"

Vernon's Sayles' Texas Civil Statutes (1914) Vol. 3, Article 4724.

Washington

"Section 6123. Number of Incorporators.

"Any number of persons, not less than seven, may incorporate a company to write insurance upon the lives of persons, and every insurance pertaining thereto, or connected therewith, and to grant or dispose of annuities or to write policies of endowment. [L. '09, p. 539, sec. 2.]"

Remington & Ballinger's Annotated Codes and Statutes of Washington, Vol. 2, sec. 6123.

West Virginia

"Life insurance companies chartered by and doing business in this State, and empowered to make contracts contingent upon life, may grant and issue annuities, either in connection with or separate from contracts of insurance predicted upon life risks, and all such annuities heretofore issued by such companies shall be valid."

West Virginia Code (1909 Supplement) sec. 1107a17.

Wisconsin

"Section 1897. An insurance corporation may be formed for the following purposes: * * *

"* * *

"(3) Life Insurance.—Upon the lives or health of persons, and every assurance pertaining thereto, and to grant, purchase or dispose of annuities and endowments." Ch. 460, Laws of Wisconsin 1909.

Wisconsin Statutes (1911) sec. 1897.

STATES WHICH SINCE 1910 HAVE CLASSIFIED LIFE INSURANCE COMPANIES AS SUCH UPON THE BASIS OF THE SALE OF LIFE INSURANCE POLICIES AND ANNUITIES

Arkansas

"Corporations may be formed or enter this State to effect insurance for the following purposes:

"* * *

"Sec. 7647. Life insurance. Upon the lives or health of persons, and every assurance pertaining thereto, and to grant, purchase or dispose of annuities and endowments."

Digest of Statutes of Arkansas (1937) Pope, Vol. II, sec. 7647.

Idaho

"40-301. Insurance classified.—All insurance business in this state is classified into fourteen classes, defined by the following sections of this chapter.

"40-304. Class 3-Life.—Life insurance, including endowments and annuities, but not including health or accident or sickness insurance, or any casualty insurance as hereinafter provided."

Idaho Code Annotated (1932) Title 40, secs. 301, 304.

Iowa

"Annuities. Any life insurance company organized on the stock or mutual plan may grant and sell annuities."

Code of Iowa (1935) Ch. 398, sec. 8673-e1.

New Hampshire

"1. Purposes. Subject to the additional or varied requirements stated in this chapter, a corporation may be formed, pursuant to the provisions of chapter 225, for the purpose of conducting the following kinds of insurance business:

"III. On the lives of persons and every insurance pertaining thereto or connected therewith, including endowments, and to grant, purchase or dispose of annuities."

Public Laws of New Hampshire (1926) Vol. 2, Ch. 272, sec. 1, III.

Utah

"Classification of Insurance Business. All insurance business in the state of Utah is hereby classified as follows:

"(1) Life insurance, including within its meaning insurance upon the lives of persons and every insurance ap-

pertaining thereto, and the granting, purchasing and disposing of annuities."

Revised Statutes of Utah (1933) Title 43, Ch. 3, sec. 2 (1).

Vermont

"General provisions. Subject to the additional or varied requirements stated in this and the eleven following sections, a corporation may be formed pursuant to the provisions of the general corporation law to do any or all insurance and reinsurance comprised in any one of the following numbered subdivisions:

"I. On the lives of persons and every insurance appertaining thereto or connected therewith, including endowments, and to grant, purchase or dispose of annuities;

"* * *"

Public Laws of Vermont (1933), Ch. 277, Insurance Companies, sec. 6911.

Wyoming

"Life insurance companies defined. All corporations, associations, partnerships, or individuals, doing business in the state under any charter, contract, agreement, or statute of this or of any other state involving the payment of money or other things of value to families or representatives of policy or certificate holders, or members, conditioned upon the continuance or cessation of human life, or involving insurance, guarantee, contract, or pledge for the payment of endowments or annuities, shall be deemed to be life insurance companies, and shall be subject to this article. [L. '21, c. 142, §23.]"

Wyoming Revised Statutes (1931) Ch. 57, sec. 223.

LETTER, FIDELITY ASSURANCE ASSOCIATION TO BANKING COMMISSION OF WISCONSIN, MARCH 24, 1941

(Exhibit 67)

Complying with your request of March 6 for an additional deposit of $51,000 to our account, we are shipping to Treasurer John M. Smith, State Treasury Department, Madison, Wisconsin, $51,000 United States Treasury ¾% Notes due Sept. 15, 1944. It is expected this shipment will go forward tomorrow.

Very truly yours,
Fidelity Assurance Association
By Hubert F. Young

CERTIFICATE OF AUDITOR AND EX OFFICIO INSURANCE COMMISSIONER AND SECRETARY OF STATE OF WEST VIRGINIA AS TO AMENDMENT OF CHARTER, CHANGE OF NAME AND LICENSING AS INSURANCE COMPANY

(Exhibit 24)

June 25, 1941

This is to certify that Fidelity Investment Association, with its principal place of business in Wheeling, West Virginia, chartered under the laws of the State of West Virginia to engage in the sale of annuity contracts on fixed and stipulated installments, made application to this office on December 31, 1940, as required under the provisions of section 3, article 2, chapter 33 of the 1931 Code of West Virginia, to change the charter powers of such corporation to include the power to engage in the life insurance busi-

ness and to change the name of the corporation from Fidelity Investment Association to Fidelity Assurance Association. These changes were approved by the Insurance Commissioner and The Honorable William S. O'Brien, Secretary of State, issued his certificate and changed the records of his office pertaining to this corporation as per the attached copy of the certificate of amendment.

Thereupon, the same date the corporation made application, copy of which is attached hereto, to the Insurance Commissioner of the State of West Virginia for a license to engage in the life insurance business as provided in article 3 of chapter 33 of the 1931 Code of West Virginia, as amended, and such license was granted, copy of which said license is also attached hereto.

On January 13, 1941, the company also made application, upon forms supplied by the Insurance Commissioner for that purpose, for the licensing of twenty-one persons to engage in the sale of life insurance policies, which said licenses were issued.

Furthermore, on January 14, 1941, the company filed, in duplicate, and secured approval for use in this state of a form titled, "Special Annuity Contract."

Also, on January 27, 1941, the company filed, in duplicate, and secured approval for use in this state of the following forms:

Ordinary Life
Ten Payment Life
Fifteen Payment Life
Twenty Payment Life
Fifteen Year Endowment
Twenty Year Endowment
Ten, Fifteen and Twenty Year Term

The company license, heretofore referred to as having been issued December 31, 1940, expired on March 31, 1941, as specified by law, and a renewal of such license was issued, dated April 1, 1941, for a term of one year, expiring March 31, 1942.

The foregoing statement is predicated upon the files and records of the office of the Insurance Commissioner in the State of West Virginia.

Given under my hand and official seal of office this 25th day of June, 1941.

Edgar B. Sims (Signed)

EDGAR B. SIMS

STATE AUDITOR & EX OFFICIO
INSURANCE COMMISSIONER

(SEAL)

STATE OF WEST VIRGINIA

(SEAL)

CERTIFICATE

I, WM. S. O'BRIEN, Secretary of State of the State of West Virginia, hereby certify that F. S. Risley, President of

FIDELITY INVESTMENT ASSOCIATION,

a corporation created and organized under the laws of the State of West Virginia, has certified to me under his signature and the corporate seal of said corporation, that, at a special meeting of the stockholders of said corporation, regularly held in accordance with the requirements of the

law of said State, at the Home Office of said corporation, in the City of Wheeling, State of West Virginia, on the 9th day of December, 1940, at which meeting a majority of the issued and outstanding voting stock of such corporation being represented by the holders thereof, in person, by bodies corporate or by proxy, and voting for the following resolutions, the same were duly and regularly adopted and passed, to-wit:

"BE IT RESOLVED,

'1. That Article 1 of the Certificate of Incorporation of the Association be amended by striking out of the name of the corporation the word 'Investment' and inserting in lieu thereof the word 'Assurance,' so that the name of the corporation after changed, shall be "Fidelity Assurance Association.'

"2. That Article 3 of the Charter, containing the purposes of the Association, be stricken out and that there be inserted in lieu thereof, as Article 3, the following purposes:

'To issue insurance upon the lives of persons and every insurance appertaining thereto and connected therewith, and to grant, purchase and dispose of annuities."

WHEREFORE, I do declare said amendment of the Certificate of Incorporation and change of name to be authorized by law, and that said corporation shall hereafter be known by the name of FIDELITY ASSURANCE ASSOCIATION.

(Signature and certification as to copy omitted.)

REPORT OF CENTRAL TRUST COMPANY, TRUSTEE, ON SECURITIES COMPRISING THE INVESTMENT PORTFOLIO OF FIDELITY ASSURANCE ASSOCIATION, FILED MAY 15, 1942

(Omitting Schedules)

In the Matter of
FIDELITY ASSURANCE ASSOCIATION,
Debtor
In Proceedings for Corporate Reorganization.
No. 4514.

TO THE HONORABLE BEN MOORE,
JUDGE OF SAID COURT:

Central Trust Company, Trustee, respectfully reports unto Your Honor that since its appointment herein on June 6th, 1941, to the date hereof, it has been continuously studying and analyzing the various securities which comprise the Portfolio. The policy adopted by your Trustee as a yardstick for measuring the advisability of handling each individual issue has been, and continues to be, in effect, that preservation of principal is the primary object and that conservation of income, although important, is secondary to the preservation of principal.

Your Trustee further respectfully reports that all of the securities, excepting United States Treasury obligations and those rated "A" or better, are regarded in the main by your Trustee as either falling in the so-called "marginal"

classification, or securities which cannot be regarded as satisfactory for investment of savings funds.

Economic conditions, as a result of the present state of emergency occasioned by a transition from what may be termed a "peace economy" to a "war economy," have, in the opinion of your Trustee, increased the risks of such a heavy concentration in marginal securities, by reason of which your Trustee has suggested to the various State Depositories the advisability of considering the sale of many securities as hereinafter more particularly set out, and your Trustee is of the opinion that a great many more such suggestions will be made in the very near future, depending upon conditions affecting individual issues which may arise from day to day.

Your Trustee further respectfully reports that the factors which it interprets as indicating the market trend of the various groups of securities classified by your Trustee as marginal, may be more specifically expressed as follows:

STATE, COUNTY, MUNICIPAL and REVENUE BONDS. In the opinion of your Trustee, there are two important influences bearing on the future of individual state and municipal securities:

(1) The uncertainty as to the permanency of tax exemptions which exerts an influence on the market value of all states and municipals; and

(2) The decrease in revenues that may result in certain states and municipalities by reason of the dislocation of industries brought about by the war.

As to the first point, the Treasury proposal before Congress involving a recommendation for the retroactive elimination of tax exemption on state and municipal securities,

although Congress has given no indication that it will comply with the Treasury proposal, there is every indication that the Treasury will continue to press for the elimination of such tax exemption on state and municipal securities at subsequent opportunities and the threat will continue to overhang the entire state and municipal bond market. Of equal importance, states and municipalities that are dependent for revenues on gasoline taxes, sales taxes, tourist trade and the like may suffer severely. To summarize, your Trustee concludes that states and municipals today are being subjected to major changes bearing on the strength of their credit position, and this applies directly to many of the state and municipal securities now held in the Portfolio of the Debtor.

Your Trustee further respectfully desires to point out that in many cases exceptionally poor markets exist for the sale of the type of state and municipal issues held in the Portfolio. Therefore, considerable time is required in disposing of these securities to the best interests of the estate. The longer the delay in acting on such vulnerable securities, just to such an extent is the danger increased that satisfactory sale can be accomplished. Reasonable selling opportunities for the middle and lower grade securities would, in the opinion of your Trustee, develop only during periods of firm to uptrending prices, and at present such a period seems to have developed from the low levels of last January and February when war and the tax threats were being widely publicized and discussed; and it is only a matter of time until these factors calling for caution again get attention.

The revenue bonds are, in the opinion of your Trustee, even more vulnerable to the factors hereinbefore mentioned for state and municipal securities, for the reason that they are not general obligations and could be classified as taxable without violating states rights.

RAILROAD BONDS. As will hereinafter appear in more detail, your Trustee has recently suggested the advisability of considering the sale of many of the marginal railroad securities held in the Portfolio and deposited with various State officials. This is because of two main factors:

(1) The price appreciation which such bonds have attained; and

(2) The uncertainty as to how long such values can be sustained under war conditions.

Such bonds have now recovered to a price level where they are again selling in the area at which liquidation by banks and other financial institutions can reasonably be expected to be greatly accelerated.

Your Trustee is of the opinion that even with a background of favorable current railroad earnings (before taxes), there can be no assurance that further substantial recoveries in such securities will come about, and, furthermore, favorable markets for such securities are only available on a firm or rising trend.

There are many potential influences which might readily cause a considerable decline in the value of these securities. First, there is the uncertainty as to the duration of the war. An earlier than generally anticipated termination of the war would, in the opinion of your Trustee, cause a great increase in the liquidation of railroad securities by investors and institutions alike. The railroad industry al-

most more than any other single classification has obtained the greatest financial benefit from the war economy. Conversely, in the post war period, it must face a serious readjustment of its traffic and earning factors. The long term outlook, particularly the threat of truck and air freight competition, further emphasizes the advisability of protecting this trust against the consequences of overstaying the present position in railroad securities.

An added factor indicating the desirability of prompt action relative to the reduction of railroad bonds is the possibility that agitation for government operation of the railroads may develop in the event there is serious congestion growing out of the increased demands on the industry because of the movement of war materials. Assuming that any such possible government operation would be on a basis of a guaranty of earnings based on a three-year average of earnings, as was the case in the last war, there would be a sharp reduction in the net earnings available to the industry as compared with the prospects for 1942 under private operation. Of particular significance is the restraint which would thus be placed on the volume of bond repurchases in the open market by the railroad companies of their own securities, thus limiting purchases from the sources generally regarded as likely to provide the major support for such bonds.

A further factor of considerable weight is the very substantial blocks of these marginal railroad bonds held in the Portfolio. Considerable time must be allowed to effect an orderly sale of such large blocks, and, therefore, in the opinion of your Trustee, it is essential that such selling action be initiated during the period of demand for this

type of security in order to assure that such sales be accomplished at satisfactory levels.

PUBLIC UTILITY BONDS. Your Trustee respectfully submits that the best opportunities for disposing of marginal utilities may already have been passed, by reason of the fact that there has been a steady decline in the market value of this portion of the Portfolio for the past several months. The major influences exerting force on the market value of these securities is the inability of the utility industry to overcome the penalty of a rising tax structure and cost of operation without a comparative increase in rates. An estimated analysis based upon the pending tax bill now before Congress indicates a 15% to 20% decline in the net earnings of the public utility industry, the variation depending on the final tax terms which may be enacted.

Of even greater importance, in the opinion of your Trustee, is the fact that a conservative estimate of future tax factors leads to the conclusion that a high normal and surtax rate structure will endure well beyond the termination of the war. Thus the current decline in the utility industry earnings must be regarded as more or less of a permanent condition, with prospects for rehabilitation of earning power in the post war period likely to be held to negligible proportions.

As previously suggested, the opportunity for the most favorable disposal of this portion of the Portfolio already may have been passed. However, the dangers of further capital loss in these public utility securities are still of sufficiently large proportions to justify aggressive action in the sale of these securities, and your Trustee further desires to emphasize the necessity of prompt action because of the

very substantial blocks involved, which require emphasis upon orderly disposition to avoid unduly depressing the market. Once the tax bill is finally enacted by Congress, and the general public begins to find the reflection of such tax penalties in published earnings, the opportunities for disposal of such issues may be still further reduced, as against the present.

INDUSTRIAL BONDS. Your Trustee respectfully suggests that there are many of the same factors operating in the case of the industrial bonds in the Portfolio as are exerting an influence in other marginal securities. A substantial portion of the industrial bonds held represents companies that rank as war beneficiaries, and as such have enjoyed a substantial temporary recovery in earning power. In numerous cases sinking fund provisions, based on a rate of earnings, have been the important contributing factor in the market conditions for such issues. It is significant that this temporary stimulus of war earnings has influenced the market conditions for many of the Portfolio industrial issues, with the result that they have only recently been selling in the open market for close to the top price in the war period, and in many instances 20 or 30 points above the levels which they might be expected to command in a peace economy. Your Trustee, therefore, respectfully suggests that such opportunities as have been presented should be realized upon in order that the preservation of the principal may thus be obtained at the satisfactory levels now prevailing.

REAL ESTATE BONDS. Your Trustee further respectfully submits that the real estate issues held in the Portfolio are, in the main, highly speculative, and in many cases

involving defaults, and are, therefore, in much the same position as other marginal securities. Some of the issues are deriving partial benefit from the war economy, and such an improvement is being reflected in the price of the individual issues. These factors, among others, would seem to dictate the desirability of prompt action, and your Trustee feels that certain of these issues should be disposed of as opportunities are presented. Here again the matter of orderly liquidation would be a paramount problem since marketability of this type of issue is exceptionally poor, thus if a decision is made to dispose of any individual issue, your Trustee will require a considerable period of time, in all probability, before a market can be found. This, of course, further substantiates the fact that prompt, rather than delayed, action is desirable.

MISCELLANEOUS BOND GROUP. The thirteen bond issues contained in the financial and foreign group represent special situations, each of which must be decided on its own merits. Action on these issues is largely a matter of price, with a view of taking advantage of such market opportunities as may develop.

PREFERRED AND COMMON STOCKS. This portion of the Portfolio represents a highly volatile group of issues, which is subject to all the uncertainties of the stock market. As such, they should be regarded as candidates for ultimate disposal. Individual decisions will depend on timing of market factors, and the individual influences, such as taxes, which affect the value of each specific security. As the spring war campaigns unfold, the price of these individual issues may readily be subjected to considerable pressure, although as a group they may be expected in turn to

respond to a possible improvement in war news to a greater extent than the bond portion of the Portfolio. Your Trustee suggests particular attention to the industrial issues which constitute the heaviest portion of the stock Portfolio. This group is constituted in substantial part in war beneficiaries, such as the steel, paper and machinery industries. In the opinion of your Trustee, it is essential that these issues be disposed of well before the termination of the war economy if a reasonable price is to be obtained.

Your Trustee further respectfully submits that the above comments have been confined to an expression of general policy rather than a discussion of individual issues. Recommendations as to individual issues are more particularly set out on a comparative summary of the Portfolio of Fidelity Assurance Association prepared by Standard & Poor's Corporation hereto attached, marked "EXHIBIT A" and prayed to be made a part hereof. This comparative summary gives the par value, book value and market value of each individual issue as of June 6, 1941, December 31, 1941, and March 31, 1942, in addition to which is a recommendation as to the disposition of each issue as of March 31, 1942.

Your Trustee further respectfully submits a schedule showing the securities recommended for sale on deposit with various States which said schedule is hereto attached, identified as "EXHIBIT B" and prayed to be made a part hereof, which said schedule shows, by States, sale recommendations complied with, sale recommendations not complied with, and as to each individual issue the book value June 6, 1941, the value as of date sale was recommended the unit price, value at date of recommendation, unit price

at date recommendation withdrawn, proceeds of sale, unit price market March 31, 1942.

Your Trustee respectfully directs Your Honor's attention to the fact that the only States which have complied with the recommendations of your Trustee are Delaware and Missouri. Illinois and Maryland each made one sale as suggested by your Trustee, and your Trustee respectfully directs Your Honor's attention to the fact that in making the sale handled by the State representative, a price from 2 to 3 points under the market at the date of recommendation was obtained by the State officials, respectively. Your Trustee does not intend to criticize the State officials, but merely desires to call attention to the fact as substantiating the position of your Trustee, to the effect that skilful handling of sales is necessary to avoid depressing the market.

Your Trustee further respectfully reports unto Your Honor that as of May 1st, 1942, it suggested to various State Depositories the advisability of selling a very substantial number of securities, all as more particularly shown by a detailed list thereof hereto attached and marked for identification purposes "EXHIBIT C" and prayed to be made a part hereof. The State of Missouri is the only depository which has complied.

As shown by the schedule hereto attached, marked "EXHIBIT D" and made a part hereof, your Trustee has, as therein set out, made purchase recommendations, and only the Delaware and Missouri depositories have complied as indicated. A very substantial loss of income is resulting thereby because of the fact that there is now available cash on deposit with the various State officials in excess of three million dollars ($3,000,000.00) as shown by a statement

thereof, by States, hereto attached and marked "EXHIBIT E," and made a part hereof.

In conclusion, your Trustee respectfully submits that in its opinion it would be for the best interests of the estate to have all the securities comprising the Portfolio of the Debtor, regardless of location, either placed in the actual custody of your Trustee or placed in the custody of the State Depositories' New York correspondent banks subject to the orders of your Trustee for the purpose of facilitating delivery against payment, and therefore recommends that a decree be made and entered herein to the foregoing effect.